Legislative Audit Division



State of Montana

Report to the Legislature

November 2005

Financial Audit

For the Fiscal Year Ended June 30, 2005

Public Employees' Retirement Board

Department of Administration A component unit of the state of Montana

We performed a financial audit of the Public Employees' Retirement Board for the fiscal year ended June 30, 2005. This report contains one recommendation concerning the actuarial soundness of the retirement systems.

Direct comments/inquiries to: Legislative Audit Division Room 160, State Capitol PO Box 201705 Helena MT 59620-1705

05-08

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FINANCIAL AUDITS

Financial audits are conducted by the Legislative Audit Division to determine if the financial statements included in this report are presented fairly and the agency has complied with laws and regulations having a direct and material effect on the financial statements. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2005, will be issued by March 31, 2006. The Single Audit Report for the two fiscal years ended June 30, 2003, was issued on March 23, 2004. Copies of the Single Audit Report can be obtained by contacting:

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November 2005

The Legislative Audit Committee of the Montana State Legislature:

This is our report on the fiscal year 2004-05 financial audit of the Public Employee's Retirement Board (PERB), a component unit of the state of Montana. The objectives of a financial audit include determining if the program's financial statements present fairly its financial position at June 30, 2005 and the results of its operations for the fiscal year. We tested compliance with state and federal laws that have a direct and material impact on the financial statements. Additional compliance testing for the program is included in our biennial financial-compliance audit of PERB. Included in this report is one recommendation related to the actuarial soundness of the three systems.

We issued an unqualified opinion on PERB's financial statements for the fiscal year ended June 30, 2005, with comparative totals for June 30, 2004. Our audit opinion on the financial statements is also contained in PERB's Comprehensive Annual Financial Report. Copies of the PERB's annual report for fiscal year 2004-05 can be obtained from the Montana Public Employee Retirement Administration (MPERA). The annual report contains background, statistical, and actuarial information that is not included in this audit report, which may be of interest to legislators or the public.

The written response to the audit recommendation is included at the end of the audit report. We thank the executive director and his staff for their assistance and cooperation throughout the audit.

Respectfully submitted,

/s/ Scott A. Seacat

Scott A. Seacat Legislative Auditor

Legislative Audit Division

Financial Audit For the Fiscal Year Ended June 30, 2005

Public Employees' Retirement Board

Department of Administration

A component unit of the state of Montana

Members of the audit staff involved in this audit were Pearl M. Allen, Chris G. Darragh, Geri Hoffman, Brenda Kedish, Paul J. O'Loughlin, and Melissa Soldano.

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Board Response	Public Employees' Retirement Board

Appointed and Administrative Officials

Public Employees' Retirement Board			Term <u>Expires</u>
	Carole Carey, President	Ekalaka	3/31/07
	Betty Lou Kasten, Vice President	Brockway	3/31/06
	Robert Griffith	Helena	3/31/08
	N. Jay Klawon	Hamilton	3/31/09
	Troy McGee	Helena	3/31/08
	Terrence Smith	Big Sky	3/31/09
	John Paull	Butte	3/31/10

Administrative Officials

Mike O'Connor, Executive Director

Kim Flatow, Member Services Bureau Chief

Roxanne Minnehan, Fiscal Services Bureau Chief

Kathy Samson, Defined Contribution Plans & Educational Services Bureau Chief

For additional information concerning the Montana Public Employees' Retirement Board, contact:

Mike O'Connor, Executive Director 100 North Park Avenue, Suite 200 PO Box 200131 Helena MT 59620-0131 (406) 444-3154

e-mail: moconnor@mt.gov

Public Employees' Retirement Board

This report contains the results of our financial audit of the Public Employees' Retirement Board (PERB) for the fiscal year ended June 30, 2005. We issued an unqualified opinion on the financial statements for the fiscal year ended June 30, 2005. This means the reader can rely on the financial information presented. The financial-compliance audit of the PERB for the two fiscal years ended June 30, 2004, was issued in a separate report (04-08).

Montana Public Employee Retirement Administration (MPERA) personnel prepare PERB financial statements from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) with adjustment. Adjustments are made to properly present financial activity.

This report contains one recommendation related to the actuarial soundness of three retirement systems. The previous financial-compliance audit report for the two fiscal years ended June 30, 2004, contained four recommendations to the PERB. Two of the four recommendations were not material to the financial statements and will be reviewed during the 2006 financial-compliance audit. The other two recommendations related to seeking legislation to ensure Public Employees' Retirement System - Defined Benefit Retirement Plan (PERS-DBRP), Sheriffs' Retirement System (SRS), and Game Wardens' and Peace Officers' Retirement System (GWPORS) are funded on an actuarially-sound basis and that PERB implement procedures to ensure mutual and fixed fund asset balances recorded on SABHRS reconcile to the external investments, were implemented. Although legislation was sought during the 2005 session, no legislation was passed to correct the funding problem.

The listing below serves as a means of summarizing the recommendations contained in the report, the department's response thereto, and a reference to the supporting comments.

Report Summary

Recommendation #1	We recommend legislation be enacted for funding changes to	
	ensure the PERS-DBRP, SRS, and GWPORS are funded on an	
	actuarially sound basis, as required by the Montana	
	Constitution.	9

Introduction

Introduction

We performed a financial audit of the Public Employees' Retirement Board (PERB) for the fiscal year ended June 30, 2005. The objectives of our audit were to:

- Determine PERB's compliance with material and direct laws and regulations which could have an effect on the financial statements.
- 2. Determine the status with direct & material prior audit recommendations.
- 3. Determine if the financial statements prepared by the Montana Public Employee Retirement Administration (MPERA) fairly present PERB's fiduciary net assets as of June 30, 2005, and the changes in fiduciary net assets for the fiscal year then ended, in conformity with generally accepted accounting principles.

The financial-compliance audit of the PERB's financial statements for the two fiscal years ended June 30, 2004, was issued in a separate report in December 2004 (04-08).

MPERA prepares PERB's financial statements from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) with adjustment. Adjustments are made to accurately present financial activity to the readers of the statements.

This report contains one recommendation. In accordance with section 5-13-307, MCA, we analyzed the cost of implementing the recommendation contained in this report and determined it was significant and is discussed in the report section.

Background

The PERB is a component unit of the state of Montana. A component unit is a legally separate organization for which the state of Montana is financially accountable. The PERB has exclusive control of the funds of eight retirement systems, including the Volunteer Firefighters' Compensation Act, as well as the Section 457 Deferred Compensation Plan. The PERB governs MPERA, which is responsible for daily administration of the retirement systems. The governor appoints the seven board members to five-year terms.

Introduction

Defined Benefit Pension Trust Funds

PERB manages the activities of the following defined benefit pension trust funds:

- ▶ Public Employees' Retirement System-Defined Benefit Retirement Plan (PERS-DBRP)
- ▶ Judges' Retirement System (JRS)
- ▶ Highway Patrol Officers' Retirement System (HPORS)
- ▶ Sheriffs' Retirement System (SRS)
- ► Game Wardens' and Peace Officers' Retirement System (GWPORS)
- ▶ Municipal Police Officers' Retirement System (MPORS)
- ▶ Firefighters' Unified Retirement System (FURS)
- ▶ Volunteer Firefighters' Compensation Act (VFCA)

These retirement systems provide pension, disability, and death benefits to eligible members. The monthly benefits are based on years of service and salary levels while still employed. The Volunteer Firefighters' Compensation Act provides pension, disability, and death benefits to volunteer firefighters who are members of eligible Montana volunteer fire companies. Monthly benefits are based on years of service.

Defined Contribution Pension Trust Funds

PERB manages the activities of the following defined contribution pension trust funds:

- ▶ Public Employees' Retirement System Defined Contribution Retirement Plan (PERS-DCRP)
- ▶ Section 457 Deferred Compensation Plan (457 Plan)

The 457 Plan allows employees to set aside and invest a portion of their salary each payday toward retirement while deferring state and federal income taxes until future years. The PERS-DCRP takes the PERS contributions attributable to the employee and allows the employee to invest the contributions at his or her discretion. Employees participating in these two plans have two investment options:

- the fixed option, which guarantees both principal (contributions) and a pre-established quarterly rate of earnings;
- the variable option, which consists of selected mutual funds.

Participating employees are allowed to invest in both the fixed and variable options. Those participating in the variable option may invest in as many offered funds as desired.

Withdrawal of deferred compensation funds is only available to employees upon separation from service, retirement, death, or upon an unforeseeable emergency meeting IRS-specified criteria while still employed. Withdrawals from PERS-DCRP are available upon termination of a PERS covered position.

Prior Audit Recommendations

The financial-compliance audit report for the two fiscal years ended June 30, 2004, contained four recommendations to the PERB. Two of the four recommendations were not material to the financial statements and will be reviewed during the 2006 financialcompliance audit. Seeking legislation to actuarially fund three of the systems and implementing procedures to ensure mutual and fixed asset balances are reconciled are the two direct and material recommendations addressed in this report. During the 2005 financial audit we determined that these recommendations were addressed. PERB has procedures in place to reconcile the mutual and fixed asset balances for the PERS-DCRP and the 457 plans; however, there are still large differences with the fixed assets in the 457 plan. PERB is continuing to look into these differences and we will follow up on their progress in further detail during the 2006 financial-compliance audit. PERB sought legislation during the 2005 Legislative Session; however, no legislation addressing the actuarial soundness of the systems was passed. Further discussion related to the systems actuarial soundness is discussed in this report beginning on page 5.

Findings and Recommendations

Three Retirement Systems Actuarially Unsound

Based on the July 1, 2005, actuarial valuations, the Public Employees' Retirement System - Defined Benefit Retirement Plan (PERS – DBRP), Sheriffs' Retirement System (SRS), and Game Wardens' and Peace Officers' Retirement System (GWPORS) are not actuarially sound, as required by the Montana Constitution and state law.

Article VIII, Section 15, of the Montana Constitution requires public retirement systems be funded on an actuarially sound basis. A defined benefit retirement system is defined in state law as being actuarially sound when its contributions are sufficient to pay the full actuarial cost of the plan over a period of up to 30 years.

The PERB obtained an actuarial valuation of each of its eight defined benefit retirement plans annually for each of the last two years. The most recent actuarial valuation was as of July 1, 2005. The PERB actuary determined the employer contribution rate would have to be increased as follows, starting January 1, 2006, to maintain an amortization of the Unfunded Actuarial Accrued Liability (UAAL) over the 30-year period:

PERS – DBRP 1.62%; from 13.80% to 15.42%; SRS 2.76%; from 18.78% to 21.54%; and GWPORS .27%; from 19.56% to 19.83%.

The current maximum UAAL systems are able to pay off over 30 years are as follows: PERS \$266.4 million; GWPORS \$4.3 million; and SRS \$(3.6) million. The negative \$3.6 million for SRS indicates that the current employer and employee contributions do not cover the current costs of the system. The UAAL for each system has grown at an increasing rate, as shown in Table 1.

		Tabl	le 1						
			Accrued Liabi	lity*					
(Expressed in Thousands) Valuation Date PERS-DBRP Years SRS Years GWPORS Years									
Valuation Date	PERS-DBRP	<u>Years</u>	<u>SRS</u>	<u>Years</u>	GWPORS	<u>Years</u>			
$7/1/2000^{a}$	(\$569,940)	30.0	(\$38,502)	30.0	(\$9,044)	30.0			
$7/1/2000\ ^{\mathrm{b}}$	(251,540)	30.0	(26,002)	30.0	(5,544)	30.0			
7/1/2002	983	0.1	(16,965)	30.0	379	\otimes			

7,586

10,889

 \otimes

 \otimes

5,100

5,453

45.9

49.5

 \otimes

 \otimes

7/1/2004

7/1/2005

466,798

540,988

Source: Compiled and/or computed by the Legislative Audit Division from actuarial reports.

The valuations for the past two years have determined the UAAL for these three systems does not amortize without an increase in contributions. The actuary has attributed the growth in the unfunded liability of the systems primarily to investment returns below the actuarial investment return assumption of eight percent for each of the three systems.

Because the underlying calculations in the actuarial valuation are long-term in nature, it is advantageous to smooth out short-term

^{*} Amounts in parenthesis indicate the systems did not have an unfunded actuarial accrued liability.

Does not include the effects of legislation passed in the 2001 Legislative session related to the GABA increase.

Recalculated to include the effects of legislation passed in the 2001 Legislative session related to the GABA increase.

Findings and Recommendations

fluctuations in the market value of assets. The asset smoothing method recognizes the gains or losses over a 4-year period. The following tables depict the gain or losses that have been or will be recognized.

Table 2

<u>Montana Public Employee Retirement Administration</u>

<u>Schedule of Investment Gain/(Loss) Recognition PERS-DBRP</u>

(Expressed in Thousands)

Fiscal	Market Value Investment Gain/(Loss)			Gain/(Loss) in Past Years		Investment Gain/(Loss) Recognized in Current Year		ment Gain/(zed in Futur	
Year	Over Expected	2001	2002	2003	2004	2005	2006	2007	2008
2001	\$ (385,081)	\$ (96,270)	\$ (96,270)	\$ (96,270)	\$ (96,270)				
2002	(425,030)		(106,258)	(106,258)	(106,258)	\$ (106,258)			
2003	(38,134)			(9,534)	(9,534)	(9,534)	\$ (9,534)		
2004	143,930				35,983	35,983	35,983	\$ 35,983	
2005	1,317					329	329	329	\$ 329
2006	*						*	*	*

* Gain / (Loss) Not yet known

Source: MPERA Personnel.

Findings and Recommendations

Table 3

Montana Public Employee Retirement Administration
Schedule of Investment Gain/(Loss) Recognition SRS
(Expressed in Thousands)

						Investment			
	Market Value					Gain/(Loss)			
	Investment					Recognized	Investm	ent Gain/	(Loss
	Gain/(Loss)		Investment	Gain/(Loss)		in Current	Recogn	nized in F	uture
Fiscal	Over]	Recognized i	in Past Years	3	Year		Years	
Year	Expected	2001	2002	2003	2004	2005	2006	2007	2008
2001	\$ (16,814)	\$ (4,204)	\$ (4,204)	\$ (4,204)	\$ (4,204)				
2002	(19,133)		(4,783)	(4,783)	(4,783)	\$ (4,783)			
2003	(1,121)			(280)	(280)	(280)	\$ (280)		
2004	6,435				1,609	1,609	1,609	\$ 1609	
2005	100					25	25	25	\$ 25
2006	*						*	*	*

* Gain / (Loss) Not yet known **Source: MPERA Personnel**

Table 4

<u>Montana Public Employee Retirement Administration</u>
<u>Schedule of Investment Gain/(Loss) Recognition GWPORS</u>
(Expressed in Thousands)

						Investment Gain/(Loss)			
Fiscal	Market Value Investment Gain/(Loss)			Gain/(Loss) in Past Years		Recognized in Current Year		ent Gain/ ized in F Years	`
Year	Over Expected		2002	2003	2004	2005	2006	2007	2008
2001	\$ (4,364)	\$ (1,091)	\$ (1,091)	\$ (1,091)	\$ (1,091)				
2002	(5,323)		(1,331)	(1,331)	(1,331)	\$ (1,331)			
2003	(179)			(45)	(45)	(45)	\$ (45)		
2004	1,941				485	485	485	\$ 485	
2005	(82)					(21)	(21)	(21)	\$ (21)
2006	*			_			*	*	*

* Gain /(Loss) Not yet known

Source: MPERA Personnel

The PERB Funding and Benefits Policy states, "Whenever, through the use of long-term cash flow projections, the amortization period of a system's unfunded liabilities is projected to exceed 30 years for two consecutive valuations and the Board cannot reasonably anticipate that the amortization period would decline without an increase in funding sources, it is the obligation of PERB to recommend to the legislature that funding be increased." PERB did seek legislation for the funding changes in the 2005 Legislative Session. However, new legislation was not enacted. PERB should work with the legislature to adopt and implement a funding change to ensure the systems are funded on an actuarially sound basis, to be in compliance with the Montana Constitution.

Recommendation #1

We recommend legislation be enacted for funding changes to ensure the PERS-DBRP, SRS, and GWPORS are funded on an actuarially sound basis, as required by the Montana Constitution and state law. Independent Auditor's Report, The Public Employees' Retirement Board's Management's Discussion and Analysis, Financial Statements, Required Supplementary Information, and Supplementary Information

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor John W. Northey, Legal Counsel



Deputy Legislative Auditors: Jim Pellegrini, Performance Audit Tori Hunthausen, IS Audit & Operations James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee of the Montana State Legislature:

We have audited the accompanying Statement of Fiduciary Net Assets – Pension Trust Funds of the Public Employees' Retirement Board, A Component Unit of the State of Montana, as of June 30, 2005 - with comparative totals for June 30, 2004, and the related Statement of Changes in Fiduciary Net Assets - Pension Trust Funds for the year ended June 30, 2005 - with comparative totals for June 30, 2004. These financial statements are the responsibility of the Public Employees' Retirement Board. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the Public Employees' Retirement Board's financial statements for the fiscal year ended June 30, 2004, and, in our report dated November 15, 2004, we expressed an unqualified opinion on the respective financial statements of the fiduciary fund activities.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Public Employees' Retirement Board as of June 30, 2005, and the changes in fiduciary net assets for the fiscal year then ended, in conformity with accounting principles generally accepted in the United States of America.

Management's Discussion and Analysis, the Schedule of Funding Progress, and the Schedule of Employer Contributions & Other Contributing Entities are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of the Public Employees' Retirement Board. The Schedules of Administrative Expenses, Investment Expenses, and Consultants; the Detail of Fiduciary Net Assets (PERS-DBRP and PERS-DBEd) and the Detail of Fiduciary Net Assets (PERS-DCRP, PERS-DCEd and PERS-DC Disability) as of June 30, 2005; and the related Detail of Changes in Fiduciary Net Assets (PERS-DBRP and PERS-DBEd) and the Detail of Changes in Fiduciary Net Assets (PERS-DCRP, PERS-DCEd and PERS-DC Disability) for the fiscal year then ended are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

At July 1, 2005, three systems, Public Employees' (PERS-DBRP), Game Warden's Peace Officer's (GWPORS) and, Sheriff's (SRS) retirement systems were not actuarially sound with an Unfunded Actuarially Accrued Liability (UAAL) totaling \$522.6 million, \$5.5 million and \$10.9 million, respectively. The maximum UAAL to comply with the amortization period of 30 years at January 1, 2006, is \$266.4 million for PERS-DBRP, \$4.3 million for GWPORS, and \$(3.6) million for SRS. The negative \$3.6 million for SRS indicates that the current employer and employee contributions do not cover the current costs of the system.

The financial statements include summarized prior-year comparative information. Such information does not include all of the information required to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Public Employees' Retirement Board's financial statements for the year ended June 30, 2004, from which such summarized information was derived.

Respectfully submitted,

/s/ James Gillett

James Gillett, CPA Deputy Legislative Auditor

October 25, 2005

The Public Employees' Retirement Board's Management's Discussion and Analysis, Financial Statements, Required Supplementary Information, and Supplementary Information

Public Employees' Retirement Board

A Component Unit of the State of Montana

Management's Discussion and Analysis

This section presents management's discussion and analysis of the Montana Public Employees' Retirement Board's financial presentation and performance of the plans administered by the Board for the year ending June 30, 2005.

Financial Highlights

- ◆ The Montana Public Employees' Retirement Board's combined total net assets of the defined benefit plans increased by \$266.5 million or 7.3 percent in fiscal year 2005. The increase was primarily due to the investment income in each of the retirement plans.
- ◆ The Montana Public Employees' Retirement Board's defined contribution plans combined total net assets increased by \$19.5 million or 8.0 percent in fiscal year 2005. The total increase in Net Assets was due to investment income and contributions in both the DCRP and the 457 plan.
- ◆ Revenues (additions to plan net assets) for the Board's defined benefit plans for fiscal year 2005 was \$467 million, which includes member and employer contributions of \$172.6 million and net investment income of \$294.4 million.
- Revenues (additions to plan net assets) for the Board's defined contribution plans for fiscal year 2005 was \$38.2 million, which includes member and employer contributions of \$21.1 million and net investment income of \$17 million.

- Expenses (deductions to plan net assets) for the Board's defined benefit plans increased from \$185.7 million in fiscal year 2004 to \$200.5 million in fiscal year 2005 or about 8 percent. The increase in 2005 is primarily due to minimal distributions for all plans, MPORS DROP distributions and an increase in total benefit recipients.
- ◆ Expenses (deductions to plan net assets) for the Board's defined contribution plans increased from \$18 million in fiscal year 2004 to \$18.9 million in fiscal year 2005 or about 4.7 percent. The increase in expenses is primarily due to an increase in distributions to terminating participants.
- ◆ The Montana Public Employees' Retirement Board's defined benefit plans funding objective is to meet long-term benefit obligations. As of July 1, 2005, the date of the latest actuarial valuation, three of the defined benefit plans were not able to pay off the unfunded liabilities over 30 years or less. As a whole the plans were actuarially funded at an average of 83.7 percent. It is important to understand this measure reflects the actuarial value of the defined benefit plans' net assets, which exceeds the actual fair value published in the financial statements. Investment earnings are critical to the defined benefit plans and the market

decline and associated investment losses in fiscal years 2001 and 2002 have had major impacts on the plans due to the smoothing of market value gains and losses over four years. The 2005 Actuarial Valuation recognizes the last part of the 2002 investments loss. The PERB introduced legislation in the 2005 Legislative Session; however, no legislation was passed to correct the funding problem. The Public Employees' Retirement Board is committed to work with the Montana Legislature to resolve the funding issues of the PERS, GWPORS and SRS.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Public Employees' Retirement Board's (PERB) financial reporting which is comprised of the following components:

- (1) Financial Statements
- (2) Notes to the Financial Statements
- (3) Required Supplementary Information

Collectively, this information presents the combined net assets held in trust for pension benefits for each of the plans administered by the Public Employees' Retirement Board as of June 30, 2005. This financial information also summarizes the combined changes in net assets held in trust for pension benefits for the year then ended. The information in each of these components is briefly summarized as follows:

(1) Financial Statements. For the fiscal year ended June 30, 2005, financial statements are presented for the fiduciary funds administered by the PERB. Fiduciary funds are used to account for resources held for the benefit of parties outside of the PERB. The fiduciary funds are held for participants in eight defined benefit plans and two defined contribution plans.

- The Statement of Fiduciary Net Assets is presented for the pension trust funds at June 30, 2005. These financial statements reflect the resources available to pay benefits to retirees and beneficiaries, at the end of the year reported.
- The Statement of Changes in Fiduciary Net Assets is presented for the pension trust funds for the year ended June 30, 2005. These financial statements reflect the changes in the resources available to pay benefits to retirees and beneficiaries, at the end of the year reported.
- (2) Notes to the Financial Statements. The Notes to the Financial Statements provide additional information that is essential for a full understanding of the data provided in the financial statements. The information in the Notes to the Financial Statements is described as follows:
 - Note A provides a summary of significant accounting policies, including the basis of accounting, capital assets and equipment used in operations, operating lease, GASB 40 Disclosures, methods used to value investments, summaries of investment vendors and other significant accounting policies or explanations.
 - Note B provides information about litigation.
 - Note C describes the debt obligation of the PERS-DCRP. The INTERCAP implementation loan for the PERS-DCRP is to be paid back over fifteen

years. The inter-entity loan from the DB Education Fund was paid off ahead of schedule in December 2004.

- Note D describes the plans' membership and descriptions of the plans administered by the Public Employees' Retirement Board. Summaries of benefits and contribution information are also provided.
- (3) Required Supplementary Information. The required supplementary information consists of the schedules of funding progress and required contributions and related notes concerning actuarial information of the defined benefit pension plans administered by the PERB.

Financial Analysis of the Systems – Defined Benefit Plans

Investments

The Montana Board of Investments (BOI), as authorized by state law, invests the defined benefit plans' assets in investment pools. Each plan owns an equity position in the pools and receives proportionate investment income from the pool in accordance with respective ownership. The investment pools are: Montana Short Term Investment Pool, Montana Domestic Equity Pool, Retirement Fund Bond Pool, Montana International Pool and Montana Private Equity Pool. Each plan's allocated share of the investment in the pools is shown in the Statement of Fiduciary Net Assets of the plan. Investment gains and losses are reported in the Statement of Changes in Fiduciary Net Assets.

Defined Benefit Plans Total Investments

At June 30, 2005, the PERB's defined benefit plans held total investments of \$3.8 billion,

an increase of \$317 million from fiscal year 2004 investment totals. On the next page are the schedules of Net Assets and Changes in Net Assets for the defined benefit plans.

Analysis of Individual Systems

PERS - DBRP and Education

The PERS-DBRP provides retirement, disability, and death benefits for covered employees of the State, local governments and certain employees of the university systems and school districts. Member and employer contributions and earnings on investments fund the benefits of the plan. The PERS-DBRP and the Education Fund have been combined in these comparisons. The PERS-DBRP net assets held in trust for benefits at June 30, 2005 amounted to \$3.2 billion, an increase of \$213 million (7 percent) from \$3.0 billion at June 30, 2004.

Additions to the PERS-DBRP net assets held in trust for benefits include employer, member, and state contributions and investment income. For the fiscal year ended June 30, contributions increased to \$127.8 million in fiscal year 2005 from \$121.3 million in fiscal year 2004, for an increase of \$6.5 million (5.4 percent). Contributions increased due to increased salaries being reported to PERS and an increased number of participating employers. The plan recognized net investment income of \$244.9 million for the fiscal year ended June 30, 2005 compared with net investment income of \$360.2 million for the fiscal year ended June 30, 2004. The decrease in investment income is mainly due to the slowing of the equity market.

Deductions from the PERS-DBRP net assets held in trust for benefits primarily include retirement benefits, refunds/distributions, administrative expenses and miscellaneous expenses. For fiscal year 2005, benefits amounted to \$142.8 million, an increase of \$10.1 million (7.6 percent) from fiscal year 2004. The increase in benefit payments was due to the increase in benefit recipients, the average recipient's benefit and distributions to participants. For fiscal year 2005, refunds/distributions amounted to \$13.7 million, an increase of \$2.4 million (20.9 percent) from fiscal year 2004. The increase in refunds/distributions was due to minimal distributions. For fiscal year 2005, the costs of administering the plan's benefits amounted to \$2.5 million, a decrease of \$256 thousand (9)

percent) from fiscal year 2004. The decrease in administrative expenses for the fiscal year 2005 was due to communications with members.

An actuarial valuation of the PERS-DBRP assets and benefit obligations is usually performed every two years. An additional valuation was performed July 2005 to provide the Legislature with updated information on the funding issues. At July 1, 2005, the date of the most recent actuarial valuation, the funded status of the plan decreased to 85.46

Fiduciary Net Assets - Defined Benefit Plans

As of June 30, 2005 - and comparative totals for June 30, 2004

(dollars in thousands)

	PE	RS	JR	S	HPO	HPORS		S
	2005	2004	2005	2004	2005	2004	2005	2004
Assets:								
Cash and Receivables	69,284	116,329	1,399	1,894	2,191	2,747	3,953	5,713
Securities Lending Collateral	140,880	141,311	2,191	2,237	3,779	3,952	6,858	6,997
Investments	3,174,677	2,914,680	47,140	43,062	81,601	75,881	147,565	134,855
Property and Equipment	1	1						
Intangible Assets	319	535	3	6	3	6	4	6
Total Assets	3,385,161	3,172,855	50,733	47,199	87,574	82,586	158,380	147,571
Liabilities:								
Securities Lending Collateral	140,880	141,311	2,191	2,237	3,779	3,952	6,858	6,997
Other Payables	862	866	7	7	28	25	52	70
Total Liabilities	141,742	142,177	2,198	2,244	3,807	3,977	6,910	7,067
Total Net Assets	3,243,419	3,030,678	48,535	44,955	83,767	78,609	151,470	140,504

Changes In Fiduciary Net Assets - Defined Benefit Plans

For the year ended June 30, 2005 - and comparative totals for June 30, 2004

(dollars in thousands)

(donars in triodsarids)								
1	PER	S	JRS	3	HPO	HPORS		S
	2005	2004	2005	2004	2005	2004	2005	2004
Additions:								
Contributions	127,861	121,298	1,574	1,579	4,855	3,950	5,801	5,369
Investment Income (Loss)	244,976	360,266	3,640	5,248	6,353	9,322	11,381	16,404
Total Additions	372,837	481,564	5,214	6,827	11,208	13,272	17,182	21,773
Deductions:								
Benefits	142,789	132,683	1,624	1,670	5,790	5,493	5,527	4,903
Refunds/Distributions	13,678	11,311			230	296	634	318
Administrative Expenses	2,569	2,825	9	14	29	31	57	55
Miscellaneous Expenses	1,073	1,484						
Total Deductions	160,109	148,303	1,633	1,684	6,049	5,820	6,218	5,276
Prior Period Adjustments	13	1,056	-1	20		26	1	12
Incr/(Decr) in Net Assets	212,741	334,316	3,580	5,163	5,159	7,478	10,965	16,509

percent from 86.72 percent at July 1, 2004. The PERS-DBRP actuarial value of assets is less than actuarial liabilities by \$540.9 million at July 1, 2005, compared with \$466.8 million at July 1, 2004. The decrease in funded status as of the last actuarial valuation is a result of the valuation recognizing the previous four-year investment performance and the time value of money associated with not actuarially funding the system.

JRS

The JRS provides retirement, disability and death benefits for all Montana judges of the district courts, justices of the Supreme Court and the Chief Water Judge. Member and employer contributions and earnings on investments fund the benefits of the plan. The JRS net assets held in trust for benefits at June 30, 2005 amounted to \$48.5 million, an increase of \$3.5 million (8.0 percent) from \$45.0 million at June 30, 2004.

GWPC	GWPORS		MPORS		FURS		A	тот	AL
2005	2004	2005	2004	2005	2004	2005	2004	2005	2004
3,415	2,695	10,396	11,155	9,760	10,467	2,086	1,705	102,484	152,705
2,296	2,209	7,083	7,143	6,725	6,801	922	963	170,734	171,613
48,458	42,584	151,478	137,323	144,044	130,726	19,552	18,433	3,814,515	3,497,544
								1	1
4	6	4	6	4	6	5		346	571
54,173	47,494	168,961	155,627	160,533	148,000	22,565	21,101	4,088,080	3,822,434
2,296	2,209	7,083	7,143	6,725	6,801	922	963	170,734	171,613
51	39	64	73	53	53	43	43	1,160	1,176
2,347	2,248	7,147	7,216	6,778	6,854	965	1,006	171,894	172,789
51,826	45,246	161,814	148,411	153,755	141,146	21,600	20,095	3,916,186	3,649,645

GWPC	GWPORS		MPORS		FURS		:A	TOTA	AL
2005	2004	2005	2004	2005	2004	2005	2004	2005	2004
5,077	4,735	13,920	13,133	12,008	11,542	1,527	1,434	172,623	163,040
3,696	5,073	11,708	16,392	11,141	15,692	1,550	2,271	294,445	430,668
8,773	9,808	25,628	29,525	23,149	27,234	3,077	3,705	467,068	593,708
1,539 613	1,460 504	11,363 798	10,885 388	10,386 101	9,674 79	1,517	1,479	180,535 16,054	168,247 12,896
42	42	65	70	53	53	47	40	2,871	3,130
						11	12	1,084	1,496
2,194	2,006	12,226	11,343	10,540	9,806	1,575	1,531	200,544	185,769
1	15	1	4	1	22	3	21	19	1,176
6,580	7,818	13,403	18,186	12,610	17,450	1,505	2,195	266,543	409,115

Additions to the JRS net assets held in trust for benefits include member and employer contributions and investment income. For the fiscal year ended June 30, 2005, contributions remained stable at \$1.6 million. The plan recognized net investment income of \$3.6 million for the fiscal year ended June 30, 2005 compared with net investment income of \$5.2 million for the fiscal year ended June 30, 2004. The decrease in investment income is mainly due to the slowing of the equity market.

Deductions from the JRS net assets held in trust for benefits mainly include retirement benefits and administrative expenses. For fiscal year 2005, benefits remained stable at \$1.6 million. The decrease in administrative expenses for the fiscal year 2005 was mostly due to communications with members.

An actuarial valuation of the JRS assets and benefit obligations is usually performed every two years. An additional valuation was performed July 2005 to provide the Legislature with updated information on the funding issues. At July 1, 2005, the date of the most recent actuarial valuation, the funded status of the plan increased to 137.73 percent from 129.98 percent at July 1, 2004. The JRS actuarial assets were more than actuarial liabilities by \$13 million at July 1, 2005, compared with \$10.4 million actuarial surplus at July 1, 2004. The increase in funded status as of the last actuarial valuation is a result of the experience of the system.

HPORS

The HPORS provides retirement, disability and death benefits for members of the Montana Highway Patrol. Member and employer contributions, registration fees and earnings on investments fund the benefits of the plan. The HPORS net assets held in trust for benefits at June 30, 2005 amounted to

\$83.7 million, an increase of \$5.1 million (6.6 percent) from \$78.6 million at June 30, 2004.

Additions to the HPORS net assets held in trust for benefits include employer, and member contributions, registration fees and investment income. For the fiscal year ended June 30, contributions increased to \$4.8 million in fiscal year 2005 from \$3.9 million in fiscal year 2004, an increase of \$905 thousand (22.9 percent). Contributions increased because the number of participating members contributing to the plan and payments received from a lawsuit settlement. The plan recognized net investment income of \$6.4 million for the fiscal year ended June 30, 2005 compared with net investment income of \$9.3 million for the fiscal year ended June 30, 2004. The decrease in investment income is mainly due to the slowing of the equity market.

Deductions from the HPORS net assets held in trust for benefits mainly include retirement benefits, refunds/distributions and administrative expenses. For fiscal year 2005, benefits amounted to \$5.8 million, an increase of \$297 thousand (5.4 percent) from fiscal year 2004. The increase in benefit payments was due to the increase in benefit recipients and the increase in the average recipient's benefit. For fiscal year 2005, refunds/distributions amounted to \$230 thousand, a decrease of \$66 thousand (22.2 percent) from fiscal year 2004. The decrease in refunds/distributions was due to distributions to fewer members.

An actuarial valuation of the HPORS assets and benefit obligations is usually performed every two years. An additional valuation was performed July 2005 to provide the Legislature with updated information on the funding issues. At July 1, 2005, the date of the most recent actuarial valuation, the funded status of the plan decreased to 72.65 percent from

76.01 percent at July 1, 2004. The HPORS actuarial assets were less than actuarial liabilities by \$31.0 million at July 1, 2005, compared with \$25.0 million at July 1, 2004. The decrease in funded status as of the last actuarial valuation is a result of the valuation recognizing the previous four-year investment performance and the experience of the system.

SRS

The SRS provides retirement, disability and death benefits for all Department of Justice criminal investigators hired after July 1, 1993 and all Montana sheriffs. Member and employer contributions and earnings on investments fund the benefits of the plan. The SRS net assets held in trust for benefits at June 30, 2005 amounted to \$151.5 million, an increase of \$10.9 million (7.8 percent) from \$140.5 million at June 30, 2004.

Additions to the SRS net assets held in trust for benefits include member and employer contributions and investment income. For the fiscal year ended June 30, contributions increased to \$5.8 million in fiscal year 2005 from \$5.4 million in fiscal year 2004, for an increase of \$432 thousand (8.0 percent). Contributions increased because the number of participating members contributing to the plan increased and the total compensation reported for active members increased. The plan recognized net investment income of \$11.4 million for the fiscal year ended June 30, 2005 compared with net investment income of \$16.4 million for the fiscal year ended June 30, 2004. The decrease in investment income is mainly due to the slowing of the equity market.

Deductions from the SRS net assets held in trust for benefits mainly include retirement benefits, refunds/distributions and administrative expenses. For fiscal year 2005, benefits amounted to \$5.5 million, an increase of \$624 thousand (12.7 percent) from fiscal year 2004. The increase in benefit payments was mainly due to an increase in benefit recipients. For fiscal year 2005, refunds/distributions amounted to \$633 thousand, an increase of \$315 thousand (99.1 percent) from fiscal year 2004. The increase in refunds/distributions was due to minimal distributions.

An actuarial valuation of the SRS assets and benefit obligations is usually performed every two years. An additional valuation was performed July 2005 to provide the Legislature with updated information on the funding issues. At July 1, 2005, the date of the most recent actuarial valuation, the funded status of the plan decreased to 93.17 percent from 94.90 percent at July 1, 2004. The SRS actuarial assets were less than actuarial liabilities by \$7.6 million at July 1, 2004, compared with \$10.9 million at July 1, 2005. The decrease in funded status as of the last actuarial valuation is a result of the valuation recognizing the previous four-year investment performance and the time value of money associated with not actuarially funding the system.

GWPORS

The GWPORS provides retirement, disability and death benefits for game wardens, warden supervisory personnel and state peace officers. Member and employer contributions and earnings on investments fund the benefits of the plan. The GWPORS net assets held in trust for benefits at June 30, 2005 amounted to \$51.8 million, an increase of \$6.6 million (14.5 percent) from \$45.2 million at June 30, 2004.

Additions to the GWPORS net assets held in trust for benefits include member and employer contributions and investment income.

For the fiscal year ended June 30, contributions increased to \$5.1 million in fiscal year 2005 from \$4.7 million in fiscal year 2004, for an increase of \$342 thousand (7.2 percent). Contributions increased because the number of members contributing to the plan increased. The plan recognized net investment income of \$3.7 million for the fiscal year ended June 30, 2005 compared with net investment income of \$5.1 million for the fiscal year ended June 30, 2004. The decrease in investment income is mainly due to the slowing of the equity market.

Deductions from the GWPORS net assets held in trust for benefits mainly include retirement benefits, refunds/distributions and administrative expenses. For fiscal year 2005, benefits amounted to \$1.5 million, an increase of \$79 thousand (5.4 percent) from fiscal year 2004. The increase in benefit payments was due to the increase in benefit recipients and the increase in the average recipient's benefit. For fiscal year 2005, refunds/distributions amounted to \$613 thousand, an increase of \$109 thousand (21.7 percent) from fiscal year 2004. The increase in refunds/distributions was largely due to the turnover rate of corrections officers.

An actuarial valuation of the GWPORS assets and benefit obligations is usually performed every two years. An additional valuation was performed July 2005 to provide the Legislature with updated information on the funding issues. At July 1, 2005, the date of the most recent actuarial valuation, the funded status of the plan increased slightly to 90.33 percent from 89.86 percent at July 1, 2004. The GWPORS actuarial assets were less than actuarial liabilities by \$5.4 million at July 1, 2005, compared with \$5.1 million at July 1, 2004. The change in unfunded liability as of the last actuarial valuation is a result of the valuation recognizing the previ-

ous four-year investment performance and the time value of money associated with not actuarially funding the system.

MPORS

The MPORS provides retirement, disability and death benefits for municipal police officers employed by first- and second-class cities and other cities that adopt the plan. Member, employer and state contributions and earnings on investments fund the benefits of the plan. The MPORS net assets held in trust for benefits at June 30, 2005 amounted to \$161.8 million, an increase of \$13.4 million (9.0 percent) from \$148.4 million at June 30, 2004.

Additions to the MPORS net assets held in trust for benefits include employer, member, and state contributions and investment income. For the fiscal year ended June 30, contributions increased to \$13.9 million in fiscal year 2005 from \$13.1 million in fiscal year 2004, for an increase of \$787 thousand (6.0 percent). Contributions increased because the total compensation reported for active members increased. The plan recognized net investment income of \$11.7 million for the fiscal year ended June 30, 2005 compared with net investment income of \$16.4 million for fiscal year ended June 30, 2004. The decrease in investment income is mainly due to the slowing of the equity market.

Deductions from the MPORS net assets held in trust for benefits mainly include retirement benefits, refunds/distributions and administrative expenses. For fiscal year 2005, benefits amounted to \$11.4 million, an increase of \$478 thousand (4.4 percent) from fiscal year 2004. The increase in benefit payments was due to the increase in benefit recipients and the increase in the average recipient's benefit. For fiscal year 2005, refunds/distributions amounted to \$798 thousand, an increase of

\$410 thousand (105.6 percent) from fiscal year 2004. The increase in refunds/distributions was largely due to DROP account distributions received by members completing their DROP period.

An actuarial valuation of the MPORS assets and benefit obligations is usually performed every two years. An additional valuation was performed July 2005 to provide the Legislature with updated information on the funding issues. At July 1, 2005, the date of the most recent actuarial valuation, the funded status of the plan increased to 57.68 percent from 57.48 percent at July 1, 2004. The MPORS actuarial assets were less than actuarial liabilities by \$116.9 million at July 1, 2005, compared with \$110.6 million actuarial liabilities at July 1, 2004. The decrease in funded status as of the last actuarial valuation is a result of the valuation recognizing the previous four-year investment performance.

FURS

The FURS provides retirement, disability and death benefits for firefighters employed by first- and second-class cities and other cities that adopt the plan, and firefighters hired by the Montana Air National Guard on or after October 1, 2001. Member, employer, and state contributions and earnings on investments fund the benefits of the plan. The FURS net assets held in trust for benefits at June 30, 2005 amounted to \$153.8 million, an increase of \$12.6 million (8.9 percent) from \$141.1 million at June 30, 2004.

Additions to the FURS net assets held in trust for benefits include employer, member, and state contributions and investment income. For the fiscal year ended June 30, contributions increased to \$12.0 million in fiscal year 2005 from \$11.5 million in fiscal year 2004, an increase of \$466 thousand (4.0 percent). Contributions increased because the number

of members contributing to the plan increased and the total compensation reported for active members increased. The plan recognized net investment income of \$11.1 million for the fiscal year ended June 30, 2005 compared with net investment income of \$15.7 million for the fiscal year ended June 30, 2004. The decrease in investment income is mainly due to the slowing of the equity market.

Deductions from the FURS net assets held in trust for benefits mainly include retirement benefits, refunds/distributions and administrative expenses. For fiscal year 2005, benefits amounted to \$10.4 million, an increase of \$712 thousand (7.4 percent) from fiscal year 2004. The increase in benefit payments was due to the increase in benefit recipients and the increase in the average recipient's benefit. For fiscal year 2005, refunds/distributions amounted to \$101 thousand, an increase of \$22 thousand (28.1 percent) from fiscal year 2004. The increase in refunds/distributions was largely due to minimal distributions.

An actuarial valuation of the FURS assets and benefit obligations is usually performed every two years. An additional valuation was performed July 2005 to provide the Legislature with updated information on the funding issues. At July 1, 2005, the date of the most recent actuarial valuation, the funded status of the plan increased to 63.57 percent from 62.44 percent at July 1, 2004. The FURS actuarial assets were less than actuarial liabilities by \$86.8 million at July 1, 2005, compared with \$85.5 million actuarial liability at July 1, 2004. The decrease in funded status as of the last actuarial valuation is a result of the valuation recognizing the previous four-year investment performance.

VFCA

The VFCA provides retirement, disability and death benefits for volunteer firefighters who

are members of eligible volunteer fire companies in unincorporated areas. State contributions and earnings on investments fund the benefits of the plan. The VFCA net assets held in trust for benefits at June 30, 2005 amounted to \$21.6 million, an increase of \$1.5 million (7.5 percent) from \$20.1 million at June 30, 2004.

Additions to the VFCA net assets held in trust for benefits include state contributions and investment income. For the fiscal year ended June 30, contributions increased to \$1.5 million in fiscal year 2005 from \$1.4 million in fiscal year 2004, an increase of \$93 thousand (6.5 percent). Contributions increased because there was an increase in the fire insurance premium taxes collected. The plan recognized net investment income of \$1.6 million for the fiscal year ended June 30, 2005 compared with net investment income of \$2.3 million for the fiscal year ended June 30, 2004. The decrease in investment income is mainly due to the slowing of the equity market.

Deductions from the VFCA net assets held in trust for benefits mainly include retirement benefits, supplemental insurance payments and administrative expenses. For fiscal year 2005, benefits amounted to \$1.5 million, an increase of \$38 thousand (2.6 percent) from fiscal year 2004.

An actuarial valuation of the VFCA assets and benefit obligations is usually performed every two years. An additional valuation was performed July 2005 to provide the Legislature with updated information on the funding issues. At July 1, 2005, the date of the most recent actuarial valuation, the funded status of the plan decreased to 69.25 percent from 69.94 percent at July 1, 2004. The VFCA actuarial assets were less than actuarial liabilities by \$9.5 million at July 1, 2005, compared

with \$8.6 million at July 1, 2004. The decrease in funded status as of the last actuarial valuation is a result of the valuation recognizing the previous four-year investment performance and a new benefit provision that allows certain members to obtain a benefit based on more than 20 years of service.

Actuarial Valuations and Funding Progress

An actuarial valuation of each of the PERB's defined benefit plans is usually performed every two years. An additional valuation was performed as of June 30, 2005 to provide the Legislature with updated information on the funding issues. At the date of the most recent actuarial valuation, June 30, 2005, the funded status of each of the plans is shown in the Schedule of Funding Progress on page A-64.

The PERB funding objective is to meet longterm benefit obligations through investment income and contributions. Accordingly, the collection of employer and member contributions, and the income from investments provide the reserves needed to finance future retirement benefits. Since investment earnings are critical to the defined benefit plans' funding, the market decline and associated investment losses in fiscal year 2000 through fiscal year 2003 have deteriorated the plans' funding. The investment losses have reduced the assets available to pay previously incurred benefit obligations. The investment losses have increased the unfunded liability of the plans. Public pension plans are considered actuarially sound if the unfunded accrued actuarial liability amortization period is less than 30 years. Montana's constitution requires that public retirement plans be funded on an actuarially sound basis.

The PERB has been concerned with the funding of three of the eight defined benefit retirement plans administered. The three plans are the PERS - Defined Benefit Retirement Plan (PERS-DBRP), the Game Wardens' and Officers' Peace Retirement System (GWPORS) and the Sheriffs' Retirement System (SRS). The PERS and GWPORS statutory contribution rates are able to pay the normal cost of the plan, but are insufficient to pay off unfunded liability. The SRS statutory contribution rate is not sufficient to pay the normal cost of the plan or the unfunded liability. Based on the PERB's June 30, 2005 Actuarial Valuations the unfunded liability in these three plans will not be amortized in 30 years. As of June 30, 2005, the estimated shortfalls in statutory contributions rates were 1.58% in PERS-DBRP, 0.26% in GWPORS, and 2.69% in SRS. The Board submitted legislation for the 2005 Legislative Session to address these insufficiencies. The legislation was not enacted.

Funding ratios range from a high of 137.73 percent to a low of 57.68 percent. The Schedule of Funding Progress on page A-64 shows the July 1, 2005 funding ratios compared with the ratios at July 1, 2004, July 1, 2002 and July 1, 2000. The table also shows the amount by which actuarial assets exceeded or fell short of actuarial liabilities. The funding ratio decline is a result of the overall investment performance of past years. The actuary performs a smoothing of investment gains/losses over a period of four years. At July 1, 2005, the actuarial value of assets was less than the market value of assets by \$76 million compared with the actuarial value of assets exceeding the market value of assets by \$21 million at July 1, 2004.

Defined Contribution Plans

The MPERA administers two defined contribution plans: The Public Employees' Retirement System - Defined Contribution Retire-

ment Plan (PERS-DCRP) and the Deferred Compensation (457) Plan. The schedules of Net Assets and Changes in Net Assets for the two defined contribution plans are on the following page.

PERS-DCRP

The PERS-DCRP is established under Section 401(a) of the Internal Revenue Code. This plan provides retirement benefits for plan members. This plan was available to all active PERS members effective July 1, 2002. All new hires to PERS have a 12-month window to file an irrevocable election to join the plan. The plan member and employer contributions and earnings on investments fund the benefits of the plan.

The PERB has received a long-term INTER-CAP loan through the Montana Department of Administration from the BOI to fund the plan start-up and implementation costs. The loan was renegotiated in 2005 and the term extended to 2018. As of June 30, 2005, the loan balance is \$1.39 million, which is reported in the financial statements as a long-term payable of \$1.38 million plus a current payable of \$10 thousand.

The plan net assets held in trust for benefits at June 30, 2005 amounted to \$24.1 million, an increase of \$4.8 million (24.9 percent) from \$19.3 at June 30, 2004.

Additions to the Defined Contribution Retirement Plan net assets held in trust for benefits include contributions and investment income. Contributions increased \$707 thousand (15.0 percent) from \$4.7 million in fiscal year 2004 to \$5.4 million in fiscal year 2005. Contributions increased because of the number of members contributing to the plan increased. The plan recognized net investment income of \$1.8 million fiscal year 2005, down from \$2.4 million in fiscal year 2004. The decrease

Fiduciary Net Assets - Defined Contribution Plans

As of June 30, 2005 - and comparative totals for June 30, 2004

(dollars in thousands)

(donard in thousands)						
	PERS-DCRP		457-PLAN		TOTAL	
	2005	2004	2005	2004	2005	2004
Assets:						
Cash and Receivables	605	365	303	408	908	773
Investments	24,948	20,480	239,143	224,376	264,091	244,856
Intangible Assets	4	6	145	157	149	163
Total Assets	25,557	20,851	239,591	224,941	265,148	245,792
Liabilities:						
Other Payables	1,448	1,553	186	192	1,634	1,745
Total Liabilities	1,448	1,553	186	192	1,634	1,745
Total Net Assets	24,109	19,298	239,405	224,749	263,514	244,047

Changes In Fiduciary Net Assets - Defined Contribution Plans

For the year ended June 30, 2005 - and comparative totals for June 30, 2004 (dollars in thousands)

(Tonaro III tirotabarres)						
	PERS-DCRP		457-PLAN		TOTAL	
_	2005	2004	2005	2004	2005	2004
Additions:				1		
Contributions	5,411	4,704	15,723	14,931	21,134	19,635
Investment Income (Loss)	1,768	2,381	15,267	16,152	17,035	18,533
Total Additions	7,179	7,085	30,990	31,083	38,169	38,168
Deductions:						
Refunds/Distributions	1,873	2,240	15,591	14,446	17,464	16,686
Administrative Expenses	231	214	289	170	520	384
Miscellaneous Expenses	256	214	698	800	954	1,014
Total Deductions	2,360	2,668	16,578	15,416	18,938	18,084
Prior Period Adjustments	-8		246	741	238	741
Incr/(Decr) in Net Assets	4,811	4,417	14,658	16,408	19,469	20,825

in investment income is mainly due to the slowing of the equity market.

Deductions from the Defined Contribution Retirement Plan net assets mainly include member refunds/distributions, administrative expenses and miscellaneous expenses. Refunds/distributions decreased from \$2.2 million in fiscal year 2004 to \$1.9 million in fiscal year 2005. The \$367 thousand decrease in refunds/distributions from 2004 to 2005 was due to members electing the plan and staying rather than taking a distribution. The costs of

administering the plan increased from \$214 thousand in fiscal year 2004 to \$231 thousand in fiscal year 2005, an increase of \$17 thousand (7.8 percent) from fiscal year 2004. The increase in administrative costs was mainly due to communications with members. Miscellaneous expenses increased from \$214 thousand in fiscal year 2004 to \$256 thousand in fiscal year 2005, an increase of \$42 thousand (19.5 percent) from fiscal year 2004. The increase in miscellaneous expenses was mainly due to an increase in membership.

Deferred Compensation (457) Plan

The Deferred Compensation Plan is established under Section 457 of the Internal Revenue Code. This plan is voluntary and provides supplemental retirement benefits for plan participants. The Deferred Compensation Plan is funded by contributions and by investment earnings. The plan net assets held in trust for benefits at June 30, 2005 amounted to \$239.4 million, an increase of \$14.7 million (6.5 percent) from \$224.8 million at June 30, 2004.

Additions to the Deferred Compensation Plan net assets held in trust for benefits include contributions and investment income. For fiscal year 2005, contributions increased from those of fiscal year 2004 from \$14.9 million to \$15.7 million, an increase of \$792 thousand (5.3 percent). Contributions increased because of the number of members participating in the plan increased largely due to an additional employer. The plan recognized net investment income of \$15.2 million for fiscal year 2005 compared with net investment income of \$16.2 million for fiscal year 2004. The decrease in investment income is mainly due to the slowing of the equity market.

Deductions from the Deferred Compensation Plan net assets mainly include member and beneficiary refunds/distributions, administrative expenses and miscellaneous expenses. For fiscal year 2005, refunds/distributions amounted to \$15.6 million, an increase of \$1.1 million (7.9 percent) from \$14.4 million at June 30, 2004. The costs of administering the plan increased from \$170 thousand in fiscal year 2004 to \$289 thousand in fiscal year 2005, an increase of \$119 thousand (70.1 percent) from fiscal year 2004. The increase in administrative costs was mainly due to 457 web system development and communications with members. Miscellaneous expenses decreased from \$800 thousand in fiscal year 2004 to \$698 thousand in fiscal year 2005, a decrease of \$102 thousand (12.7 percent) from fiscal year 2004. The decrease in miscellaneous expenses was mainly due the Board decreasing fees for the 457 plan participants.

Public Employees' Retirement Board

A Component Unit of the State of Montana
Statement of Fiduciary Net Assets - Pension Trust Funds as of June 30, 2005 - with comparative totals for June 30, 2004

	PERS-DBRP	JRS	HPORS	SRS	GWPORS	MPORS
Assets						
Cash and Short-term Investments	\$ 59,798,8	43 1,289,157	1,983,058	3,446,471	3,298,651	2,250,937
Securities Lending Collateral (Note A5)	140,879,5	22 2,190,613	3,778,801	6,858,241	2,296,311	7,082,770
Receivables						
Interest	7,466,2	05 110,020	189,862	344,440	115,108	355,380
Accounts Receivable	1,423,5	43	3	162,023		84,947
Due from Other Funds	293,1	26				
Due from Primary Government	135,8	67	17,953		672	7,704,884
Advances to Other Funds						
Notes Receivable	166,9	12				
Total Receivables	9,485,6	53 110,020	207,818	506,463	115,780	8,145,211
Investments, at fair value (Note A5)						
Montana Domestic Equity Pool (MDEP)	1,529,417,9	61 22,749,120	39,376,418	71,277,772	23,111,430	72,390,335
Retirement Fund Bond Pool (RFBP)	930,369,1	90 14,655,060	25,243,575	45,890,070	15,471,422	47,394,936
Montana International Pool (MTIP)	505,111,7	09 7,506,898	13,034,581	23,456,641	7,705,293	24,555,374
Montana Private Equity Pool (MPEP)	150,594,5	03 2,228,865	3,946,191	6,940,554	2,170,181	7,137,953
Equity Index Fund	1	40				
Real Estate Investments	8,525,4	00				
Mortgages & Commercial Loans						
net of Accumulated Mortgage Discount	50,658,0	46				
Defined Contributions Fixed Investments						
Defined Contributions Variable Investments						
Deferred Compensation Life Insurance						
Total Investments	3,174,676,9	49 47,139,943	81,600,765	147,565,037	48,458,326	151,478,598
Capital Assets						
Property and Equipment, at cost,						
net of Accumulated Depreciation (Note A2)	9	75				
Intangible Assets, at cost,						
net of Amortization Expense (Note A2)	318,9	75 3,000	3,247	4,043	4,083	3,942
Total Capital Assets	319,9	50 3,000	3,247	4,043	4,083	3,942
Total Assets	3,385,160,9	17 50,732,733	87,573,689	158,380,255	54,173,151	168,961,458
Liabilities						
Securities Lending Collateral Liability	140,879,5	22 2,190,613	3,778,801	6,858,241	2,296,311	7,082,770
Accounts Payable	439,5	54 87	1,593	93	12,444	4,275
Due to Other Funds	56,6	88 6,626	25,923	52,236	37,606	59,282
Due to Primary Government	46,3	34				
Advances from Primary Government (Note C)						
Advances from Other Funds						
Deferred Revenue	55,4	88		14	809	570
Compensated Absences	264,4	58				1(
Total Liabilities	141,742,0	44 2,197,326	3,806,317	6,910,584	2,347,170	7,146,907
Net Assets Held in Trust for Pension Benefits						

	Defined Ben	efit Pension Plans		Defined C	ontribution Plans		
		Total Defined			Total Defined	Total Pension	Total Pension
		Benefit			Contribution	Trust Funds	Trust Funds
FURS	VFCA	Pension Plans	PERS-DCRP	457 Plan	Plans	2005	2004
0.047.400		70 755 404	540.005	202.405	054 200	77 000 574	422 202 007
2,647,168	2,040,899	76,755,184	548,285	303,105	851,390	77,606,574	123,303,807
6,725,272	922,258	170,733,788				170,733,788	171,612,792
337,479	46,232	8,964,726				8,964,726	12,471,304
56,228	10,202	1,726,744	14	11	25	1,726,769	1,662,558
		293,126	56,688		56,688	349,814	378,209
6,718,625		14,578,001				14,578,001	15,248,844
							85,500
		166,912				166,912	326,441
7,112,332	46,232	25,729,509	56,702		56,713	25,786,222	30,172,856
00.044.070	0.000.044	4 000 000 400				4 000 000 400	4 762 772 606
68,911,373	9,096,014	1,836,330,423 1,130,169,094				1,836,330,423	1,763,773,625 982,191,950
44,974,935 23,360,926	6,169,906 3,293,974	608,025,396				1,130,169,094 608,025,396	521,777,657
6,797,319	991,926	180,807,492				180,807,492	154,636,871
0,737,313	331,320	140				140	23
		8,525,400				8,525,400	8,409,210
		0,020,100				4,550,750	5,100,210
		50,658,046				50,658,046	66,755,267
			1,545,772	149,791,530	151,337,302	151,337,302	144,076,550
			23,401,771	89,338,924	112,740,695	112,740,695	100,767,440
				12,316	12,316	12,316	12,316
144,044,553	19,551,820	3,814,515,991	24,947,543	239,142,770	264,090,313	4,078,606,304	3,742,400,909
		975				975	1,436
3,661	4,580	345,531	4,464	145,305	149,769	495,300	732,554
3,661	4,580	346,506	4,464	145,305	149,769	496,275	733,990
160,532,986	22,565,789	4,088,080,978	25,556,994	239,591,191	265,148,185	4,353,229,163	4,068,224,354
						100000000000000000000000000000000000000	454 646 566
6,725,272	922,258	170,733,788	42 200	405 703	470.024	170,733,788	171,612,792
91 49 795	43 142	458,164 330,288	13,308	165,723	179,031 19,525	637,195	638,762
48,785	43,142	330,288 46,334	14,647 30,697	4,878 4,021	34,718	349,813 81,052	378,209 82,567
			1,380,195	4,021	1,380,195	1,380,195	1,390,195
			1,000,100		1,500,155	1,000,100	85,500
3,756		60,637			-	60,637	57,549
2,. 20		264,468	8,801	11,291	20,092	284,560	286,313
6,777,904	965,427	171,893,679	1,447,648	185,913	1,633,561	173,527,240	174,531,887
153,755,082	21,600,362	3,916,187,299	24,109,346	239,405,278	263,514,624	4,179,701,923	
100,100,002	21,000,002	0,010,101,203	24,100,040	200,700,210	200,014,024	4,119,191,023	3,000,002,401

Public Employees' Retirement Board

A Component Unit of the State of Montana

Statement of Changes in Fiduciary Net Assets - Pension Trust Funds for the year ended June 30, 2005 - with comparative totals for June 30, 2004

	PERS-DBRP	JRS	HPORS	SRS	GWPORS	MPORS
Additions				_ 		
Contributions (Note D)						
Employer	\$ 60,297,089	1,162,148	3,323,903	2,812,818	2,053,538	3,790,841
Plan Member	66,913,560	394,157	862,268	2,975,171	3,014,857	2,424,336
Membership Fees	140					
Interest Reserve Buyback	72,550	17,211	4	12,532	8,499	273
Retirement Incentive Program	154,058					
Registration Fee Collections			668,748			
Miscellaneous Revenue	2,811			131		
State Contributions	420,658					7,704,884
Nonvested Member Forfeitures						
Total Contributions	127,860,866	1,573,516	4,854,923	5,800,652	5,076,894	13,920,334
Investments (Note A5)						
Net Appreciation (Depreciation)						
in Fair Value of Investments	151,817,678	2,317,474	3,790,457	7,250,833	2,310,199	7,438,204
Interest	77,935,054	1,094,574	2,164,409	3,415,053	1,157,389	3,546,287
Dividends	19,775,193	293,114	511,964	918,388	293,169	932,723
Investment Expense	(4,778,075)	(68,429)	(119,992)	(213,745)	(68,381)	(219,939
Net Invesiment Income	244,749,850	3,636,733	6,346,838	11,370,529	3,692,376	11,697,275
Securities Lending Income						
Securities Lending Income	3,224,315	50,206	87,125	156,866	51,619	162,399
Securities Lending Rebate and Fees	(2,998,456)	(46,747)	(81,113)	(146,052)	(48,072)	(151,186
Net Securities Lending Income	225,859	3,459	6,012	10,814	3,547	11,213
Total Net Investment Income	244,975,709	3,640,192	6,352,850	11,381,343	3,695,923	11,708,488
Total Additions	372,836,575	5,213,708	11,207,773	17,181,995	8,772,817	25,628,822
Deductions (Note D)				,		
Benefits	142,789,016	1,623,746	5,789,603	5,527,472	1,538,595	11,362,959
Refunds/Distributions	13,236,058		180,822	611,528	607,022	785,660
Refunds to Other Plans	441,716		49,401	21,629	6,378	12,323
Transfers to DCRP	914,334					
Transfers to ORP	158,616					
Supplemental Insurance Payments						
Administrative Expenses	2,569,385	9,122	29,222	56,743	41,642	65,469
Miscellaneous Expenses						
Total Deductions	160,109,125	1,632,868	6,049,048	6,217,372	2,193,637	12,226,411
Net Increase (Decrease)	212,727,450	3,580,840	5,158,725	10,964,623	6,579,180	13,402,411
Net Assets Held in Trust for Pension Benef	its					
Beginning of Year	3,030,678,813	44,955,415	78,608,711	140,504,020	45,246,250	148,410,720
Prior Period Adjustment	12,610	(848)	(64)	1,028	551	1,420
End of Year	\$ 3,243,418,873	48,535,407	83,767,372	151,469,671	51,825,981	161,814,551

	Defined Benef	fit Pension Plans		Defined Co	ntribution Plans		
		Total Defined			Total Defined	Total Pension	Total Pension
		Benefit			Contribution	Trust Funds	Trust Funds
FURS	VFCA	Pension Plans	PERS-DCRP	457 Plan	Plans	2005	2004
2,959,095		76,399,432	1,856,440	54,999	1,911,439	78,310,871	74,725,840
2,329,777		78,914,126	3,183,893	15,500,874	18,684,767	97,598,893	90,201,441
		140				140	130
		111,069				111,069	860,740
		154,058				154,058	431,759
		668,748				668,748	348,137
3		2,945	178,431	167,142	345,573	348,518	395,880
6,718,625	1,527,264	16,371,431				16,371,431	15,577,477
			192,257		192,257	192,257	135,246
12,007,500	1,527,264	172,621,949	5,411,021	15,723,015	21,134,036	193,755,985	182,676,650
7,070,862	838,907	182,834,614	1,112,489	8,989,779	10,102,268	192,936,882	255,513,506
3,380,873	615,819	93,309,458	655,661	6,737,702	7,393,363	100,702,821	177,697,383
887,898	123,321	23,735,770				23,735,770	20,563,392
(209,361)	(29,820)	(5,707,742)		(460,883)	(460,883)	(6,168,625)	(4,906,905
11,130,272	1,548,227	294,172,100	1,768,150	15,266,598	17,034,748	311,206,848	448,867,376
154,878	21,741	3,909,149				3,909,149	1,808,150
(144,193)	(20,239)	(3,636,058)				(3,636,058)	(1,474,610
10,685	1,502	273,091		-	-	273,091	333,540
11,140,957	1,549,729	294,445,191	1,768,150	15,266,598	17,034,748	311,479,939	449,200,916
23,148,457	3,076,993	467,067,140	7,179,171	30,989,613	38,168,784	505,235,924	631,877,566
		,,	1,11,0,11,1		20,100,101	000,000,000	001,011,000
10,385,891	1,517,098	180,534,380				180,534,380	168,247,317
101,235		15,522,325	1,873,378	15,591,355	17,464,733	32,987,058	28,962,095
		531,447				531,447	619,715
		914,334				914,334	1,295,269
		158,616				158,616	188,331
	11,100	11,100				11,100	12,000
53,367	46,594	2,871,544	230,682	289,215	519,897	3,391,441	3,514,625
			255,844	698,238	954,082	954,082	1,014,436
10,540,493	1,574,792	200,543,746	2,359,904	16,578,808	18,938,712	219,482,458	203,853,788
12,607,964	1,502,201	266,523,394	4,819,267	14,410,805	19,230,072	285,753,466	428,023,778
141,146,207	20,095,323	3,649,645,459	19,298,045	224,748,963	244,047,008	3,893,692,467	3,463,752,081
911	2,838	18,446	(7,966)	245,510	237,544	255,990	1,916,608
153,755,082	21,600,362	3,916,187,299	24,109,346	239,405,278	263,514,624	4,179,701,923	3,893,692,467

Public Employees' Retirement Board

A Component Unit of the State of Montana

Notes to the Financial Statements

for the Fiscal Years Ended June 30, 2005 and 2004

The Public Employees' Retirement Board (PERB) administers ten retirement plans and the related member education plans. The retirement plans are eight defined benefit plans and two defined contribution plans. The defined benefit retirement plans are the Public Employees' Retirement System (PERS-DBRP), Judges' Retirement System (JRS), Highway Patrol Officers' Retirement System (HPORS), Sheriffs' Retirement System (SRS), Game Wardens' and Peace Officers' Retirement System (GWPORS), Municipal Police Officers' Retirement System (MPORS), Firefighters' Unified Retirement System (FURS), and the Volunteer Firefighters' Compensation Act (VFCA). The defined contribution retirement plans are the Public Employees' Retirement System (PERS-DCRP) and the Deferred Compensation (IRC §457) Plan. The PERS-DCRP was implemented July 1, 2002. All PERS new hires after July 1, 2002 have a twelve-month window from their date of hire to file an election. The Deferred Compensation Plan is available to employees of the state, university and local political subdivisions that contract with the plan.

PERS members are provided member education as a tool to help them decide between participation in the Defined Benefit Retirement Plan (PERS-DBRP) or the Defined Contribution Retirement Plan (PERS-DCRP). If members are employees of the university system they have a third choice, the Optional Retirement Program (ORP). The plan choice is a one-time irrevocable election. Education is also available for the members who choose

the PERS-DCRP. This education includes information on investment choices.

The assets of each plan are maintained separately, including member education funds, and may be used only for the payment of benefits to the members and administrative expenses of the appropriate plan, in accordance with the terms of each plan as prescribed in Title 19, of the Montana Code Annotated (MCA). The financial statements are presented by combining the PERS-DBRP and the DBRP Education Fund and by combining the PERS-DCRP, the DCRP Education Fund and the DCRP Disability Fund. A presentation of each individual fund is shown at the end of the financial section.

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. BASIS OF ACCOUNTING

The PERB is a discretely presented component unit Pension Trust Fund of the State of Montana financial reporting entity. The Montana Public Employee Retirement Administration (MPERA), staff of the PERB, prepares the accounting records and financial statements for the fiduciary/pension trust funds using the accrual basis of accounting. For the pension trust funds, member contributions are recognized in the period in which contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Revenues are recognized in the accounting period in which they are earned and become measurable. Benefits and refunds/distributions are recognized in the accounting period in which they are due and payable. Expenses are recognized in the period incurred. Administrative expenses are financed through investment earnings on the pension trust fund for the defined benefit plans. Interfund receivables and payables exist at year-end because all defined benefit administrative expenses are accounted for within PERS-DBRP and then allocated to the other defined benefit plans at year-end.

Adjustments to the fiscal year 2005 financial statements consist of prior period adjustments to all defined benefit plans and the DCRP for a reallocation of administrative expenses for all years since the implementation of the DCRP. Adjustments to the 457 plan include an entry made to balance the variable annuity based on the reconciliation process.

Participants of the PERS-DCRP are charged, on a quarterly basis, a flat fee plus a basis point fee on their account balance. The flat fee covers the recordkeeping provided by Great West Retirement Services (Great West). The basis point fee is returned to the PERB to cover the PERB's administrative expenses of the plan. The fees returned to the PERB are recorded as *Miscellaneous Revenue* in the financial statements.

Participants of the deferred compensation (457) plan are charged fees, quarterly, based on individual account balances. The record keeper, Great West, withholds fees and after payment of the Great West's contractual expenses, the excess fees are remitted to the PERB. The excess fees, recorded as *Miscellaneous Revenue*

in the financial statements, are used to pay the PERB's related administrative expenses.

2. CAPITAL ASSETS AND EQUIPMENT USED IN OPERATIONS

Assets under \$5,000 are expensed in the year purchased. Assets valued at \$5,000 or more, are recorded at cost less straight-line depreciation over the estimated useful life of five to ten years. Equipment for the MPERA consists of a microfiche reader/printer, capital assets include the web-based employer reporting software and the MPERA Website.

The accumulated depreciation on our web based reporting system is \$926,170 and \$625,560, respectively as of June 30, 2005 and 2004. The carrying value as of June 30, 2005 and 2004 is \$291,768 and \$575,515, respectively. For the 457 web based employer-reporting system the accumulated depreciation is \$43,867 and \$3,341, respectively as of June 30, 2005 and 2004. The carrying value as of June 30, 2005 and 2004 is \$137,175 and \$3,341, respectively. The accumulated depreciation on our MPERA website is \$1,422 and the carrying value is \$66,856.

3. OPERATING LEASE

Operating leases are rental agreements where the payments are chargeable as rent and recorded as administrative expenses. The MPERA entered into a 10-year lease for office space in November 2003 at the location of 100 North Park. The lease is payable monthly and includes inflationary adjustments over the period of the lease.

4. GASB 40 DISCLOSURES

Effective June 30, 2005, the Montana Board of Investments (BOI), Department of Commerce, implemented the provisions of the Governmental Accounting Standards Board (GASB) Statement No. 40 – Deposit and Investment Risk Disclosures. The definition of the investment risk disclosures are as follows:

Credit Risk is defined as the risk that an issuer or other counterparty to an investment will not fulfill its obligation.

Custodial Credit Risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party.

Concentration of Credit Risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. Investments issued or explicitly guaranteed by the U.S. government are excluded from the concentration of credit risk requirement.

Interest Rate Risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

Foreign Currency Risk is the risk that changes in exchange rates will adversely affect the fair value of an investment.

If applicable, investment risks are disclosed within the investment summaries that begin on this page.

5. METHOD USED TO VALUE INVESTMENTS

The BOI invests the defined benefit retirement plan assets on behalf of the defined benefit plans. According to Article VIII, Section 13 of the Montana Constitution and 19-2-504. MCA the PERB has fiduciary responsibility for the pension funds. Investments are purchased in accordance with the statutorily and constitutionally mandated "prudent expert principle." Investments are reported at fair value. As of June 30, 2005, there were five major diversified pools, the same number as in fiscal year 2004, Montana Short Term Investment Pool (STIP), Montana Domestic Equity Pool (MDEP), Retirement Funds Bond Pool (RFBP), Montana International Pool (MTIP), and Montana Private Equity Pool (MPEP).

The PERS-DCRP and the deferred compensation plan's fixed assets were invested and managed on behalf of the plans by Pacific Investment Management Company (PIMCO)/State Street Bank Kansas City (SSKC). The third party record keeper, Great West Retirement Services, tracks and reports the daily trading and valuations of all investment options including the assets held by the individual mutual fund companies. In addition to the laws cited above, the PERS-DCRP is also governed by 19-3-2122, MCA and there are separate investment policies for the 401(a) defined contribution and 457 deferred compensation plans. The investment policies are reviewed on an annual basis and the investment options are reviewed at least annually by a third party. In the review, each investment alternative is compared to its peers and the appropriate benchmark. In addition, each investment alternative is reviewed for other indicators including, but not limited to, style drift, duplication, fund manager or other organizational changes. Investment alternatives that are determined to have a sub-standard performance rating or other negative indicators may be recommended for probation or termination. Investments are reported at fair value as of June 30, 2005.

The following are the PERB summaries of the BOI's fiscal year end statements, the PIMCO/SSKC contract and a statement about the variable investments.

STIP portfolio may include asset-backed securities, commercial paper, corporate and government securities, repurchase agreements and variable-rate (floatingrate) instruments. These securities provide a diversified portfolio earning a competitive total rate of return. Funds may be invested for relatively short periods. State agencies are legally required to invest in STIP and the PERB elects to have all STIP income automatically reinvested. Investments are reported at fair value based on market prices supplied to the BOI by the BOI's custodial bank. The unit value is fixed at \$1.00. A purchased unit earns income on the purchase date and ceases to earn income on the day before the unit is sold. STIP income reflects the monthly earnings of the STIP portfolio and is distributed on the first calendar day of the month, with the exception of the June distribution. Income for June is distributed on the last calendar day of the month. Administrative expenses incurred by the BOI are charged daily to STIP based on their expenses applicable to STIP. STIP did not participate in any securities lending transactions in fiscal years 2005 and 2004. STIP is considered an external investment pool per the Governmental Accounting Standards Board (GASB) Statement No. 31 and is classified as a "2a7-like" pool. STIP is not registered with the Securities and Exchange Commission (SEC) but does operate in a manner consistent with SEC rules. Credit Risk is that the issuer of a STIP security may default in making timely principal and interest payments. Obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. STIP securities have credit risk as measured by major credit rating services. STIP investments are required to have the highest rating in the short-term category by at least one Nationally Recognized Statistical Rating Organization (NRSRO). The table below displays all STIP investments for the State of Montana. The PERB portion of STIP is 4 percent. Investments are categorized to disclose credit rate risk as of June 30, 2005. If a security investment type is unrated, the quality type is indicated by NR (not rated). As an external investment pool, STIP has not been rated by the NRSRO. For Custodial Credit Risk as of June 30, 2005 and 2004, all the investments were registered in the nominee name for the BOI and held in the possession of the BOI's custodial bank, State Street Bank. According to the STIP Investment Policy "repurchase agreements

			Credit
Security Investment Type		Fair Value	Quality
(in thousands)		2005	Rating
Commercial Paper	\$	1,249,527	A1
Corporate Fixed		49,821	A1+
Corporate Variable-Rate		414,952	Al+
Municipal Variable-Rate		6,000	NR
Repurchase Agreement		22,000	<u>A3</u>
Total Investments	\$	1,742,300	A1+
	•		
Securities Lending			
Collateral Investment Pool	\$	0	NR

require electronic delivery of U.S. Government Treasury collateral, priced at 102 percent market value, to the designated State of Montana Federal Reserve Bank account." Concentration of Credit Risk as of June 30, 2005, - there were no single issuer investments that exceeded 5% of the STIP portfolio. The STIP Investment Policy Statement does not specifically address concentration of credit risk. The policy does provide for "minimum 3 percent or \$15 million, whichever is higher, to be invested in Repurchase Agreements." Interest Rate Risk disclosures are not required for "2a7-like" pool. Corporate asset-backed securities are based on cash flows from principal and interest payments on underlying auto loan receivables, credit card receivables and other assets. These securities, while sensitive to prepayments due to interest rate changes, have less credit risk than securities not backed by pledged assets. While variablerate (floating-rate) securities have credit risk identical to similar fixed-rate securities, their interest rate risk is more sensitive to interest rate changes. However, their fair value may be less volatile than fixed-rate securities because their value will usually remain at or near par as a result of their interest rates being periodically reset to maintain a current market vield. STIP security transactions are recorded as of the trade date rather than the settlement date. Because of this generally accepted practice, the STIP portfolio at June 30 may include receivables from brokers for securities sold, but not delivered, and payables to brokers for securities purchased, but not received. There are no legal risks that the BOI is aware of regarding any STIP investments.

MDEP portfolio may include common stock, equity index, preferred stock, convertible equity securities, American Depositary Receipts and equity derivatives. The MDEP was established in April 2003. Effective May 1, 2003, the Public Employees', Judges', Highway Patrol Officers', Sheriffs', Game Wardens' and Peace Officers', Municipal Police Officers', Firefighters' Unified and Volunteer Firefighters' retirement funds transferred all the Barclays Global Investors (BGI) S&P 500 Equity Index Fund A and the Dimensional Fund Advisors (DFA) Small Cap Subtrust investments totaling \$740 million, at cost, from the All Other Funds portfolio to the new pool. The pensions also exchanged their investment in the Montana Stock Pool (MTCP) for units in the new MDEP. In July 2003, the BOI closed the STIP account and a Stock Performance Index Futures Fund (SPIFF) account was opened to securitize MDEP cash by investing in an equity derivative. The value of MDEP units purchased and sold by participants is the result of an asset allocation decision and pool participant's cash needs. Investments are presented at fair value. Unit values are calculated weekly and at the close of the last business day of the month. Equity investments, on valuation date, are stated at the closing price of the security's primary exchange. Depending on stock market conditions and the investment officer's decision, MDEP participants may then buy or sell units on the first calendar day of each month. MDEP security transactions are recorded as of trade date rather than settlement date. Because of this generally accepted practice, the MDEP portfolio at June 30 may include receivables from brokers for securities sold but not delivered, and payables to brokers for securities purchased but not received. For Custodial Credit Risk as of June 30, 2005 and 2004, all the MDEP securities were registered in the nominee name for the BOI and held in the possession of the BOI's custodial bank, State Street Bank. The BGI, S&P 500 Equity Index Fund A, S&P 400 MidCap Equity Index Fund and the DFA Small Cap Subtrust are registered in the name of the Montana BOI. Concentration of Credit Risk as of June 30, 2005 and 2004, - there were no single issuer investments that exceeded 5% of the MDEP portfolio.

On October 11, 2002, the BOI received a summons and complaint regarding the bankruptcy of Owens-Corning. The company seeks a determination that the dividend payments paid from October 1996 through July 2000 represent "fraudulent transfers under Chapter 11 Bankruptcy provisions and applicable state law, and are, therefore, voidable". The complaint states the BOI was the "recipient of dividends in the amount of \$357,099 for the relevant period". The BOI has prepared a response to the complaint.

RFBP portfolio includes corporate securities, foreign government bonds, U.S. government direct-backed, U.S. government indirect-backed and cash equivalents. RFBP investments are presented at fair value. Fair values are determined, primarily, by reference to fair market prices supplied to the BOI by its custodial bank, State Street Bank. Premiums and discounts are amortized/accreted using the straight-line or scientific method to the call, average life or maturity date of the securities. Unit values are calculated weekly and at month end, based on portfolio pricing, to allow for participant transactions to occur as determined by the BOI's staff. The June 30, 2005 unit value

of \$105.31 increased from the June 30, 2004 unit value of \$104.32. The yield on bonds decreased during the fiscal year, which has the effect of increasing bond prices and the pool unit value. The pension funds were rebalanced in fiscal year 2005 to adjust the portfolios towards the stated equity/fixed income allocation. RFBP security transactions are recorded as of the trade date rather than the settlement date. Because of this generally accepted practice, the RFBP portfolio at June 30 may include receivables from brokers for securities sold, but not delivered, and payables to brokers for securities purchased, but not received. Accumulated income is distributed monthly on the first calendar day of the month. Realized portfolio gains/losses are distributed at least annually. Administrative expenses incurred by the BOI are charged daily to RFBP based on applicable BOI expenses. Credit Risk is that the issuer of a fixed income security may default in making timely principal and interest payments. RFBP fixed income investments are required to be rated an investment grade as defined by Moody's or by S&P rating services. Refer to the table on the following page. Obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. For Custodial Credit Risk as of June 30, 2005 and 2004, all the investments were registered in the nominee name for the BOI and held in the possession of the BOI's custodial bank, State Street Bank. The State Street repurchase agreement was purchased in the State of Montana BOI name. As of June 30, 2005 the RFBP had Concentration of Credit Risk exposure to the Federal Home Loan Mortgage Corp of 6.21%. As of June 30, 2004, there were no single issuer

investments that exceeded 5% of the RFBP portfolio. According to the RFBP Investment Policy, "with the exception of the U.S. government indirect-backed securities, additional RFBP portfolio purchases will not be made if the credit risk exceeds 2 percent of the portfolio at the time of purchase". The RFBP investment policy does not formally address Interest Rate Risk. In accordance with GASB Statement No. 40, the BOI has selected the effective duration method to disclose interest rate risk. The table below displays RFBP investments for the State of Montana. The PERB portion of RFBP is 61 percent. If a bond investment type is unrated, the quality type is indicated by NR (not rated). Both the credit quality ratings and duration have been calculated excluding cash equivalents. If duration has not been calculated, duration is indicated by NA (not applicable).

Corporate asset-backed securities are based on cash flows from principal and

		Credit	
Security Investment	Fair Value	Quality	Effective
Type (in thousands)	2005	Rating	Duration
Corporate Bonds			
(Rated)	\$ 894,556	A-	5.75
Corporate Bonds			
(Unrated)	19,538	NR	4.07
Foreign Government			
Bonds	5,218	BBB	6.67
U.S. Government			
Direct-Backed	188,790	AAA	4.50
U.S. Government			
Indirect-Backed	605,801	AAA	3.91
State Street			
Repurchase Agrmt	9,924	AA-	NA
Short Term			
Investment Pool	112,478	<u>NR</u>	<u>NA</u>
Total Fixed Income			
Investments	\$ 1,836,305	AA-	4.95
Securities Lending			
Collateral Investment			
Pool	\$ 214,243	NR	NA

interest payments on underlying auto loan receivables, credit card receivables and other assets. These securities, while sensitive to prepayments due to interest rate changes, have less credit risk than securities not backed by pledged assets. The RFBP portfolio holds REMICs (Real Estate Mortgage Investment Conduits) totaling \$554,309 and \$1,034,466 in amortized cost, respectively, as of June 30, 2005 and June 30, 2004. These securities are based on separate or combined cash flows from principal and interest payments on underlying mortgages. The interest-only (IO) are more sensitive to prepayments by mortgagees resulting from interest rate changes than other REMIC securities. The IO REMIC securities purchased in August and September 1992 are being reduced periodically towards zero according to the expected average life of the underlying mortgages. The IO securities amortized cost is \$3 as of June 30, 2005 and \$250,000 as of June 30, 2004.

As of June 30, 2005, Delta Airlines Corp. presented a higher credit risk to the BOI. The RFBP holds \$3 million par 10.0% Delta Airlines Corp. bond maturing June 5, 2013, a \$1.971 million par 10.0% Delta Airlines Corp. bond maturing June 5, 2011 and a \$6 million par 10.14% Delta Airlines Corp. bond maturing August 14, 2012. Due to a weak credit outlook and potential bankruptcy, the Board stopped the interest income accruals after the December 2004 and February 2005 pay dates. Although the interest accruals were stopped, the Board received the interest due in June 2005 and August 2005. The combined book value of these securities was \$11 million as of June 30, 2005. Due to the company's filing for Chapter 11 bankruptcy protection on September 14, 2005, the book values were reduced to \$1.5 million, \$985,500 and \$3 million, respectively.

As of June 30, 2005, Northwest Airlines Inc. presented a higher credit risk to the BOI. The RFBP held a \$9.9 million par 6.81% Northwest Airlines Inc. bond maturing February 1, 2020, a \$7.8 million par 7.935% Northwest Airlines Inc. MBIA Insurance Corp. insured bond maturing April 1, 2019 and a \$5.7 million par 4.64% Northwest Airlines Inc. real estate backed bond maturing July 7, 2010. The combined book value of these securities was \$22.9 million as of June 30, 2005. On September 14, 2005, the company filed for Chapter 11 bankruptcy protection. Due to this action, the BOI stopped the interest income accruals for the 6.81% bond maturing February 1, 2020 after the August 2005 pay date. This issue was sold on September 20, 2005 generating a loss of \$642,183. The sale included accrued interest from August 1, 2005 to September 20, 2005. Since the 7.935 bond maturing April 1, 2019 is insured by MBIA Insurance Corp. to support the payment of any interest due and outstanding principal balance, the BOI did not stop the interest income accrual or reduce book value. The 4.64% bond maturing July 7, 2010 is secured by Northwest Airlines Inc.'s corporate headquarters' building and land.

As of June 30, 2005 and June 30, 2004, Burlington Industries, Inc. presented legal and higher credit risks to the BOI. The BOI owns a Burlington Industries, Inc., \$6 million par, 7.25% bond maturing September 15, 2005. In September 2000, the company announced a reduction of stockholders equity. Due to an increasing senior bank line and declining credit trend, the bond ratings for this issue were

downgraded, in May 2001, by the Moody's and Standard & Poor's rating agencies. During fiscal year 2001, the book value of Burlington Industries Inc. was reduced from the August 31, 2000 book value of \$5.6 million to \$2.4 million. Due to the company's filing for Chapter 11 bankruptcy protection on November 11, 2001, the book value was reduced to \$1.2 million. In October 2003, Burlington Industries, Inc. received court approval to sell its assets. Under the company's recovery plan, the BOI received \$1.5 million in August 2004 for its unsecured claim. This transaction reduced the book value to \$0 and generated a gain of \$255,000. In February 2005 and May 2005, the BOI received an additional \$209,000 and \$194,000, respectively for this unsecured claim. The BOI is expected to receive additional proceeds for over the next two to three years.

As of June 30, 2004, Winn Dixie presented a higher credit risk to the BOI. The RFBP held a Winn Dixie Trust, \$70 million par, zero coupon bond maturing September 2, 2024. Due to a weak credit outlook and collateral uncertainty, the BOI stopped accruing income and reduced the book value to \$5.2 million in February 2004. On February 21, 2005, Winn Dixie declared bankruptcy. On February 28, 2005, the Board sold the bonds and recorded a \$4.6 million gain.

The BOI received a summons and complaint, dated September 3, 2002, regarding the sale of a Pennzoil Quaker State, \$5 million par, 6.75% corporate bond maturing April 1, 2009. Deutsche Bank Securities claims a "breach of contract" for the March 25, 2002 sale of the bond at a price of \$94.669 plus accrued interest. Deutsche Bank Securities seeks damages

of \$538,632 for the additional costs incurred to acquire the bond from third parties, plus any statutory interest, costs and expenses. On October 1, 2002, Shell Oil Company acquired Pennzoil and subsequently announced a public tender of Pennzoil Quaker State debt. The BOI tendered the Pennzoil Quaker State holdings on October 8, 2002 at a price of \$113.099. The tender was accepted with a settlement date of November 1, 2002. On November 4, 2002, the BOI received \$5.7 million in principal and interest plus \$150,000 as a consent fee. As of September 23, 2005, this matter is still pending.

MTIP portfolio includes equities with five externally managed funds at June 30, 2005: Pyrford International, Schroder Investment Management NA, Nomura Asset Management U.S.A. Inc., Barclays Global Investors, and Dimensional Fund Advisor Inc. (DFA). The BOI discontinued the internally managed fund, BOI Internal International, in January 2004 and on October 30, 2003, the BOI voted to replace SG Yamaichi Asset Management, Co. as an active manager with Nomura Asset Management U.S.A., Inc. The change was effective December 1, 2003. On October 21, 2004, the BOI authorized the investment in DFA. The funds invest in securities of foreign-based corporations listed on legal and recognized foreign exchanges as well as domestic exchanges. Because transactions are recorded as of the trade date rather than settlement date, the MTIP portfolio may include receivables from brokers for securities sold, but not delivered, and payables to brokers for securities purchased, but not received. Investments are presented at current U.S. dollar value after conversion from foreign currency by the custodial bank, State Street Bank and Trust. Unit values are calculated weekly and once a month at the close of the last business day of the month, based upon the fair value of the MTIP equity holdings, other assets and liabilities. Based on the BOI Investment Officer's decision, participants are allowed to buy or sell units on the first business day of each month. Realized gains/losses from the sale of securities and related foreign exchange transactions are retained by each fund. MTIP income is distributed at least monthly to the retirement funds, net of external manager fees and administrative expenses, on the first business day of the following month. For Custodial Credit Risk as of June 30, 2005 and 2004, all MTIP securities were registered in the nominee name for the Montana BOI and held in the possession of the BOI's custodial bank, State Street Bank. The BGI MSCI Europe and Pacific Index and the DFA Small Company Portfolio are registered in the name of the Montana BOI. Foreign Currency Risk is that changes in exchange rates will adversely affect the fair value of an investment. The MTIP has significant investments in 19 foreign countries. Future economic and political developments in these countries could adversely affect the liquidity or value or both of the securities in which MTIP is invested. The table on the following page discloses the investments by currency and investment type in U.S. dollars. The PERB portion of MTIP is 61 percent.

MTIP Cash by Cur	rre	nev
		Fair Value
Cash (in thousands)		2005
Australian Dollar	\$	130
Hong Kong Dollar		125
France Euro		-
Japanese Yen		1,438
South Korean Won		4
Malaysian Ringgit		7
New Zeland Dollar		68
Philippine Peso		3
Singapore Dollar		1
Swiss Franc		-
New Taiwan Dollar		193
Total Cash	\$	1,969
	-	
MTIP Investment by Se	cur	ity Type
Security Investment Type		Fair Value
(in thousands)		2005
BGI MSCI Europe Index	\$	466,247
BGI MSCI Pacific Index		50,628
BGI Cash and Money Market		-
DFA International Small Co.		76,554
SPIFF		2,111
Schroder Investment Mgmt		137,134
Pyford International		149,790
Nomura Asset Mgmt U.S.A.,		
Inc		111,054
Total Investments	\$	993,518
Securities Lending Collateral	•	
Investment Pool	\$	34,537

MPEP portfolio includes venture capital, leveraged buyout, mezzanine, distressed debt, special situation and secondary investments. The MPEP was established in April 2002 to allow retirement funds the opportunity to participate in the venture capital and leveraged buyout markets and other private equity investments via a diversified pool. MPEP cash is invested in an equity derivative, the State Street Stock Performance Index Futures Fund (SPIFF). Given the complexity and specialization of private equity investment,

the BOI contracts with ten private equity managers. The private equity managers include Adams Street Partners (formerly Brinson Partners); Kohlberg, Kravis, Roberts and Company (KKR); Welsh Carson Anderson and Stowe; Madison Dearborn Partners; Lexington Partners; Oaktree Capital Management; Arc Light Energy Partners; Inter Mountain Private Equity Partners; Odyssey Investment Partners and Carlyle Partners. Investments are presented at fair value and because no recognized market exists for private equity investment, the investments, on valuation date, are stated at the fair value reported in the most recent external managers' valuation reports. The pool portfolio will be priced quarterly. Unit values are calculated at month end and participant transactions will most likely occur on a quarterly basis. Based on the BOI Investment Officer's decision, participants are allowed to buy, reinvest or sell units on the first business day of each month. Administrative expenses incurred by the BOI are charged daily to the MPEP based on the BOI's expenses applicable to MPEP. Private equity investments are recognized as investments with a higher degree of risk with a higher return potential. Portfolio diversification of risk is to be achieved through multiple partnership relationships and investments diversified by time, financing stage, industry sector, investment size and geographical region. Private equity investments typically have a low correlation relative to other investment asset classes and should contribute to reduction of portfolio risk. For Custodial Credit Risk as of June 30, 2005 and 2004, all MPEP investments were recorded in the name of the Montana BOI. The State Street Bank and Trust repurchase agreement for \$447,174, as of June 30, 2005 was purchased in the BOI's name. This repurchase agreement was collateralized at \$458,263 by a AAA rated Federal Home Loan Mortgage Corporation note maturing February 15, 2006. Foreign Currency Risk includes several MPEP investments that represent limited partnership investments in various foreign countries. Per GASB Statement No. 40, no foreign currency risk disclosure is required for these limited partnership investments. The Montana BOI is a limited partner in the private equity partnership of O'Donnell & Masur L.P., which invested in Gardiner Communications, Inc. All partners received a Notice of Liability from the Internal Revenue Service claiming unpaid federal corporate taxes for Gardiner Communications, Inc. As a recipient of the distributions on the sale and dissolution of Gardiner Communications, Inc., the BOI faced potential liability. O'Donnell & Masur L.P. retained legal counsel to represent all partners receiving a Notice of Liability. On September 5, 2003, legal counsel filed a petition on the Montana BOI's behalf in U.S. Tax Court to perfect the right to contest this matter. On February 9, 2004, all partners of O'Donnell & Masur L.P. were informed that the Internal Revenue Service Appeals Officer had completed his review of the Gardiner Communications, Inc. matter. The Officer concluded "no additional taxes are due from Gardiner Communications, Inc. and thus, no transferee liability to the partners of O'Donnell & Masur, L.P." MPEP does not participate in securities lending.

All Other Funds (AOF) Investments are owned by various State of Montana agencies and managed on their behalf by the BOI. The portfolio for the pension plans include equity index, real estate, mortgages and commercial loans. Fair values

are determined, primarily, by reference to market prices supplied to the BOI by its custodial bank, State Street Bank and Trust. The real estate investments and residential and multifamily mortgages are valued based on a discounted cash flow. Premiums and discounts are amortized/ accreted using the straight-line or scientific method to the call, average life or maturity date of the securities. Amortized cost may also be referred to as book value. The mortgages and commercial loans receivable consist of residential mortgages and multifamily commercial loans. In November and December 2004, the multifamily commercial loans were sold to the Coal Severance Tax Trust Fund. As of June 30, 2005, Positive Systems, Inc. had an outstanding loan balance of \$546,074. With the exception of this loan, there were no other uncollectible account balances for Montana mortgages and loans receivable. As of June 30, 2004, there were no uncollectible account balances for mortgages and commercial loans funded by the retirement systems. Real estate investments held, in part, for the PERS include buildings at 100 North Park Avenue in Helena, MT; a newly constructed building at 2273 Boot Hill Court in Bozeman, MT; a building at 2401 Colonial Drive in Helena, MT; and property located on California Street in Helena, MT. The BOI also holds the building located at 1712 Ninth Avenue in Helena, MT for the sole benefit of the PERS.

Credit Risk is that the issuer of a fixed income security may default in making timely principal and interest payments. The BOI's policy requires AOF fixed income investments to be rated an investment grade as defined by Moody's and/or S&P's rating services. The U.S. govern-

ment securities are guaranteed directly or indirectly by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. The credit ratings provided are by S&P's rating services or if not available, by Moody's. For Montana mortgages, there is a lien on the real estate property. In the event of default, the property can be sold. Custodial Credit Risk as of June 30, 2005 has all Equity Index, Real Estate, Mortgage and Loan investments registered in the name of the Montana BOI. Concentration of Credit Risk is not addressed in the investment policy statements. The single issuer for residential mortgages would be the residential borrower and there are no single issuers that have a principal balances in excess of 5 percent. Investments issued or explicitly guaranteed by the U. S. government and investments by various state agencies, in the AOF portfolio, are excluded from the concentration of credit risk requirement. Interest Rate Risk is not formally addressed in the AOF investment policies. In accordance with GASB Statement No. 40, the BOI has selected the effective duration method to disclose interest rate risk. As of June 30, 2005, the AOF portfolio did not hold any structured financial instruments know as REMICs. As of June 30, 2004, the AOF portfolio held a REMIC with an amortized cost of \$15,585,949 as reported in the U.S. government mortgage-backed category. These securities are passthrough vehicles for multiclass mortgagebacked securities. The REMIC securities are based on separate or combined cash flows from principal and interest payments on underlying mortgages. When underlying mortgages are prepaid, the interest cash flows are reduced while principal cash flows are increased. If homeowners pay on mortgages longer than anticipated, the cash flow effect would be the opposite.

Securities Lending Collateral, governed under the provisions of state statutes, authorizes the custodial bank, State Street Bank and Trust, to lend the BOI's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. This is accomplished by the BOI via a Securities Lending Authorization Agreement. During the period the securities are on loan, the BOI receives a fee and the custodial bank must initially receive collateral equal to 102 percent of the fair value of the loaned security and maintain collateral equal to not less than 100 percent of the fair value of the loaned security. The BOI retains all rights and risks of ownership during the loan period. During fiscal years 2005 and 2004, State Street Bank and Trust loaned, on behalf of the BOI, certain securities held by State Street Bank and Trust, as custodian, and received U.S. dollar currency cash, U.S. government securities, irrevocable bank letters of credit. State Street Bank and Trust does not have the ability to pledge or sell collateral securities unless the borrower defaults. The BOI did not impose any restrictions during fiscal year 2005 and 2004 on the amount of the loans that State Street Bank and Trust made on its behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during fiscal years 2005 and 2004. Moreover, there were no losses during fiscal years 2005 and 2004 resulting from a default of the borrowers or State Street. During fiscal years 2005 and 2004, the BOI and the borrowers maintained the right to terminate all securities lending transactions

demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified plan lenders, in a collective investment pool, the Securities Lending Quality Trust. The relationship between the average maturities of the investment pool and the BOI's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the BOI could not determine. At year-end, the BOI has no Credit Risk exposure to borrowers because the amounts the BOI owes the borrowers exceed the amounts the borrowers owe the system. For MDEP as of June 30, 2005, the carrying and fair values of the underlying securities on loan were \$28.7 million and \$28.4 million, respectively. The cash collateral provided for the securities on loan totaled \$29 million. For RFBP as of June 30, 2005, the carrying and fair values of the underlying securities on loan were \$199.1 million and \$208 million, respectively. The cash collateral provided for the securities on loan totaled \$214.2 million. For MTIP as of June 30, 2005, the carrying and fair values of the underlying securities on loan were \$34.5 million. The cash collateral provided for the securities on loan totaled \$34.5 million. For All Other Funds as of June 30, 2005, the carrying and fair values of the underlying securities on loan were \$213.8 million and \$217 million, respectively. The collateral provided for the securities on loan totaled \$200 million in cash and \$23.6 million in collateral.

Fixed Investments are administered through outside vendors Pacific Investment Management Company (PIMCO) and custodial bank State Street Bank Kansas City (SSKC). When participants

invest in the fixed investment they are guaranteed a rate of return. The fixed investment employs a synthetic stable value strategy where the investment manager manages a diversified bond portfolio and the third party insurer guarantees the participants principal investments and earnings. The third party insurer resets the rate of return each quarter.

The PERS-DCRP fixed money is invested in a PIMCO mutual fund. The deferred compensation fixed investment is a separately managed fund that is benchmarked against the Lehman Intermediate Government/Credit/Yankee index with a duration not to exceed four years. The minimum average portfolio quality must be an Arating; the minimum issue quality must be a BB-rating and the minimum commercial paper quality must be A2/P2. The quality ratings applied are the higher of Moody's, Standard & Poor or Fitch. PIMCO has the discretion to invest in a broad array of public and private asset classes and investment vehicles including: money market instruments; U.S. Treasury and Agency notes and bonds; municipal bonds; corporate securities; Yankee and Euro bonds; mortgagebacked securities; mortgage derivatives; asset-backed securities; convertible securities; non-U.S. dollar denominated securities; non-leveraged structured notes; futures; options; swaps; credit default swaps and PIMCO pooled funds. All investments including those with derivative characteristics are reported at fair value. PIMCO may not invest in: caps and floors; preferred stock; emerging market securities; event-linked bonds and bank loans. Concentration of Credit Risk is not addressed in the investment policy; however, principal and rate of return are guaranteed for participants.

Variable Investments are held and managed by a selection of retail and institutional mutual funds, which cover all standard asset classes and categories. The selection of offered mutual funds is designed to provide plan participants with the ability to diversify and meet their individual investment goals and strategies. The PERB, with the advice of the statutorily created Employee Investment Advisory Council and the assistance of an independent contracted third-party consultant and investment analyst, conducts an annual review of the offered mutual funds. The goal of the annual review is to ensure the offered mutual funds meet standards established in the Investment Policy Statement adopted by the PERB. investment policy states "Participants make individual investment decisions, subject to the investments offered under the plan and, ultimately, bear the risks and rewards of investment returns." In the annual review, each investment alternative is compared to its peers and the appropriate benchmark. In addition, each investment alternative is reviewed for other indicators including, but not limited to, style drift, duplication, fund manager or other organizational changes. Investment alternatives that are determined to have a sub-standard performance rating or other negative indicators may be recommended for probation or termination. During the annual review, the PERB may decide to retain, replace or place in a watch status, any of the offered mutual funds. Concentration of Credit Risk is not addressed in the investment policy and investments in mutual funds are not required to be disclosed.

Investments are reported at fair value as of June 30, 2005. Available mutual funds are listed on pages A-56 and A-59 or a

listing can be obtained by contacting the MPERA.

B. LITIGATION

Each of the plans administered by the PERB may be involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management and legal counsel, the disposition of most of the matters will not have a material, adverse affect on any plan's financial position as a whole. The potential effects of the cases discussed below have not been determined.

A lawsuit, Baumgardner v. PER Board (Cause No. ADV-2002-450, First Judicial District), has been filed challenging the constitutionality of that portion of Chapter 149, L. of 2001 which, in the definition of "actuarial equivalent", substituted "the mortality table and interest rate assumptions adopted by the Board" for "the 1971 Group Annuity Mortality Table, with ages set back 4 years and an interest rate of 8% compounded annually". This amendment was effective March 29, 2001. Subsequent to the legislation, effective July 1, 2001, the Public Employees' Retirement Board adopted new actuarial assumptions, including new mortality tables, resulting in new actuarial equivalent option factors. The legal challenge is the use of these new actuarial equivalent option factors in determining the actuarial equivalent benefit payout when a single life benefit is converted to an alternate form of benefit payment. The plaintiff seeks recalculation of benefit payments and attorney's fees. The action was filed by a PERS member, but could affect other systems where members have the option to choose a benefit payment other than for the member's life only.

Three constitutional claims have been made: 1) that the legislation contained more than one subject matter, not properly reflected in the title; 2) that the legislation was an unconstitutional delegation of legislative authority; and 3) that the legislation constituted an unconstitutional impairment of contract. The district court dismissed the first claim; found in favor of the plaintiff on the second claim; and has not ruled on the third claim. The district court's ruling on the second issue was reversed by the Montana Supreme Court (Cause No. 04-861) and the case has been returned to the district court on remittitur. Requested amendments allowing two additional claims (violation of equal protection and noncompliance with the Montana Administrative Procedure Act in the adoption of the new option factors) also have not been ruled on by the district court.

An adverse decision would have different actuarial consequences depending on the claim and the breadth of the court's holding. If the holding is only that the new mortality table is an unconstitutional impairment of contract, then use of the mortality table specified in statute prior to March 29, 2001 would probably have a minimal actuarial impact on the system.

Accurately assessing the chances of ultimately prevailing on the remaining claim and all possible amendments is very difficult due to the complexity of the issues presented and status of the case.

Bean, et al v. Montana and MPERA (Cause No. ADV-2004-707, First Judicial District) challenges the constitutionality of Chapter 290, L. of 2001 which allowed firefighters hired by the Montana Air National Guard on or after October 1, 2001

to join the Firefighters Unified Retirement System (FURS) rather than the Pub-Employees' Retirement System (PERS). Plaintiffs, hired before October 1, 2001, claim the law is a violation of equal protection and seek coverage under FURS. A counterclaim seeks proper **FURS** employee contributions from plaintiffs if they are determined to be covered by FURS. A motion for summary judgment has been filed by the state and MPERA. The chance of plaintiffs prevailing is remote. The actuarial impact on the PERS and FURS has not been determined, however, a material actuarial impact of an adverse decision is remote.

Hall v. State of Montana and the Public Employees' Retirement Board (Cause No. 05-124, Montana Supreme Court) is on appeal from a district court decision dismissing a FURS equal protection claim on a statute of limitation basis. A plaintiff's chance of prevailing on the statute of limitations issue is reasonably possible. However, any plaintiff's chance of prevailing on the equal protection claim is remote. Consequently, a material actuarial impact is remote.

Internal Revenue Service Voluntary Correction Program Filing (September 7, 2005). MPERA has identified an employer who has claimed as compensation the amounts paid for group insurance that were not paid by employees through a properly administered IRC Section 125 plan. This procedure was used for the employer's PERS, MPORS, and FURS contributions for a number of years. MPERA has identified other employers who may have recently made similar insurance payments and is investigating to determine if the payments were reported as compensation and if the employers have properly

administered Section 125 plans.

The compensation would be appropriately reportable if proper indicia were met, primarily if the premiums were paid through an appropriately established and administered IRC Section 125 plan and treated as compensation for all purposes. The identified employer is proposing a selfcorrection plan for its Section 125 plan, which, if acceptable to the IRS and applied to all affected employers, would settle the issue without unanticipated financial consequence to the pension funds. The Board has filed a Voluntary Correction Program Filing with the IRS, to seek approval of the Board's acceptance of the employer's self-correction plan. The precise actuarial consequences of contribution overpayment (if that is determined to have occurred), as offset by consequent unfunded liability, have not been calculated. The probability of a net material, adverse affect on any plan's financial position as a whole is remote.

C. DEBT OBLIGATIONS

The PERS defined contribution retirement plan has an implementation loan through the Department of Administra-

tion, with the BOI. Authorization for the INTERCAP loan was provided by the Legislature, Chapter 471, Laws of 1999. Five draws were taken in the total amount of \$1,498,000. Interest repayments began immediately following the draws. Principal repayments began August 15, 2003, the year following the DCRP implementation date. The loan was renegotiated as a single sum in fiscal year 2004 to be repaid over a period of 15 years. The interest rate is variable and changes every February, impacting the interest due on the outstanding principal balance. The financial statements report the long-term payable in Advances from Primary Government for the amount \$1,380,195. The additional \$10,000 is reported in Due to Primary Government as a current payable.

The PERS-DCRP previously reported an inter-entity loan in the amount of \$114,000 that was originated on August 18, 2003. The loan was paid off ahead of schedule in December 2004.

Debt service requirements (principal and interest) for the defined contribution plan are explained in this chart:

	Sched	ule of	Debt Rep	payn	nent		
		INTE	RCAP Loai	n			
Fiscal Year							
Ended	Ended Rate*		rincipal	1	nterest	Total	
2006	3.80%	\$	10,000	\$	52,732	\$	62,732
2007	3.80%		20,000		52,256		72,256
2008	3.80%		30,000		51,260		81,260
2009	3.80%		40,000		50,303		90,303
2010	3.80%		50,000		48,548		98,548
2011-2018	3.80%	1	,240,195		244,566	1	,484,761
		\$ 1	,390,195			\$ 1	,889,860

D. PLAN MEMBERSHIP, DESCRIPTIONS AND CONTRIBUTION INFORMATION

The plans are established and amended statutorily by the Legislature. In all defined benefit plans (except VFCA), if a member leaves covered employment before retirement, the member contributions plus accrued interest may be refunded to the member. If a member returns to service and repays the withdrawn contributions plus the interest the contributions would have earned had they remained on deposit, membership service is fully restored.

Membership of each plan as of June 30, 2005 and June 30, 2004 is detailed in the following charts:

	PERS	-DBRP M	lembership		
	2005	2004		2005	2004
Number of participating employers	530	526			
Active plan members	28,213	28,201	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	14,579	14,205
Vested	2,418	2,362	Disability Retirements	338	336
Non-vested	8,153	9,132	Survivor Benefits	303	293
	10,571	11,494	•	15,220	14,834

JRS Membership									
	2005	2004		2005	<u>2004</u>				
Number of participating employers	1	1							
Active plan members	50	50	Retirees and beneficiaries receiving benefits						
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	47	48				
Vested	4	4	Disability Retirements	-	-				
Non-vested	-	-	Survivor Benefits	2	2				
	4	4	-	49	50				

HPORS Membership										
	2005	2004		2005	<u>2004</u>					
Number of participating employers	1	1								
Active plan members	201	194	Retirees and beneficiaries receiving benefits							
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	258	258					
Vested	10	8	Disability Retirements	8	7					
Non-vested	9	11	Survivor Benefits	10	9					
	19	19		276	274					

SRS Membership									
	<u>2005</u>	2004		<u>2005</u>	<u>2004</u>				
Number of participating employers	56	56							
Active plan members	680	662	Retirees and beneficiaries receiving benefits						
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	291	275				
Vested	42	41	Disability Retirements	34	34				
Non-vested	81	73	Survivor Benefits	15	14				
-	123	114	-	340	323				

	GWP	ORS Me	embership		
	<u>2005</u>	<u>2004</u>		<u>2005</u>	<u>2004</u>
Number of participating employers	8	8			
Active plan members	711	685	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	91	82
Vested	22	18	Disability Retirements	-	-
Non-vested	81	95	Survivor Benefits	3	3
	103	113		94	85

MPORS Membership					
	<u>2005</u>	<u>2004</u>		<u>2005</u>	2004
Number of participating employers	22	22			
Active plan members	605	603	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	532	531
Vested	26	20	Disability Retirements	15	13
Non-vested	35	38	Survivor Benefits	28	27
-	61	58	_	575	571

	FU	RS Mem	bership		
	<u>2005</u>	2004		2005	2004
Number of participating employers	15	15			
Active plan members	444	438	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	477	468
Vested	13	10	Disability Retirements	3	5
Non-vested	50	48	Survivor Benefits	24	25
-	63	58	_	504	498

	VF	CA Mem	bership		
	<u>2005</u>	<u>2004</u>		<u>2005</u>	<u>2004</u>
Active plan members	2,754	2,687	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits			Service Retirements	959	940
Vested	687	671	Disability Retirements	-	-
			Survivor Benefits	7	4
			_	966	944

PERS-DCRP Membership					
	<u>2005</u>	<u>2004</u>		<u>2005</u>	<u>2004</u>
Number of participating employers	230	229			
Active plan members	1136	915	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Benefit Payments	10	2
Vested	61	61	Disability Payments	-	-
Non-vested	93	57	Survivor Payments	3	-
	154	118		13	2

De	ferred C	ompensa	tion (457) Membership		
	<u>2005</u>	<u>2004</u>		2005	<u>2004</u>
Number of participating employers	10	9	Number of participating plan members	7,759	8,069
Number of participating employers that provide contributions on members' behalf	1	1	Number of participating plan members that are actively contributing to their deferred compensation accounts	5,281	5,316

Public Employees' Retirement System-DBRP (PERS-DBRP)

Plan Description: The PERS-defined benefit retirement plan (DBRP) is a multiple-employer, cost-sharing plan established July 1, 1945, and governed by Title 19, chapters 2 & 3, Montana Code Annotated (MCA). This plan covers the State, local governments and certain employees of the university system and school districts.

All new hires are initially members of the PERS-DBRP. New hires have a 12-month window during which they may choose to remain in the PERS-DBRP or join the PERS-DCRP. Members may not be members of both the *defined contribution* and *defined benefit* retirement plans. The choice is irrevocable. All new hires of the universities also

have a third option to join the university system's Optional Retirement Program (ORP). For members that choose to join the PERS-DCRP or the ORP, a percentage of the employer contribution will be used to maintain the funding of the PERS-DBRP.

The PERS-DBRP provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are established by state law and can only be amended by the Legislature. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits follows:

PERS-DBRP Summary of Benefits

Member's highest average compensation (HAC)

Highest average compensation during any consecutive 36 months

Eligible for benefit

Service retirement:

30 years of membership service, any age; Age 60, 5 years of membership service; or Age 65, regardless of service Early retirement, actuarially reduced: Age 50, 5 years of membership service; or Any age, 25 years of membership service

Vesting 5 years of membership service

Monthly benefit formula

Less than 25 years of membership service: 1.785% of HAC per year of service credit; 25 years of membership service or more: 2% of HAC per year of service credit

Guaranteed Annual Benefit Adjustment (GABA)

After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of other adjustments to the member's benefit

At June 30, 2005 PERS had 530 participating employers, an increase of 4 from FY2004. The participating employers consist of:

PEI	RS-DBRP EMPLOYERS	
<u>Employers</u>	June 30, 2005	June 30, 2004
State Agencies	35	35
Counties	55	55
Cities and Towns	95	94
Colleges and Universities	5	5
School Districts	238	237
High Schools	5	5
Other Agencies	<u>97</u>	<u>95</u>
Total	530	526

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal year 2005 was 6.9% of PERS-covered payroll, the same as in fiscal year 2004. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a request for retirement or refund is processed. Each state agency and university system employer contributed 6.9% of PERScovered payroll during fiscal years 2005 and 2004. Participating local governments and school district employers contributed 6.8% of PERS-covered payroll during fiscal years 2005 and 2004. The State contributed the remaining 0.1% for local governments and school district employers from the state general fund in fiscal years 2005 and 2004. A percentage of the employers' contributions is used to fund the employee education program. (Reference Schedule of Contribution Rates on page A-63).

Plan Membership Elections: MPERA has also included in the financial statements transfers of \$914,000 to Transfers to DCRP and \$159,000 to Transfers to ORP. These transfers reflect the DCRP and ORP contributions of participants that filed elections at or near the June 30th cutoff date but the contributions were moved in early fiscal year 2006.

PERS-DBRP Membership by Employer Type					
Employer Type	June 30, 2005	June 30, 2004			
State Agencies	10,549	10,528			
Counties	5,526	5,470			
Cities	3,002	3,012			
Universities	2,642	2,561			
High Schools	56	60			
School Districts	5,312	5,404			
Other Agencies	1,126	1,166			
Total	28,213	28,201			

Additional Service Purchase: A provision (19-2-706, MCA) related to the Employee Protection Act allows state and university system employees, who are eligible

for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-5" additional service. As of fiscal year 2005, 323 employees had taken advantage of this provision since its inception, up from 308 in fiscal year 2004. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. The retirement incentive contributions received (including interest) during fiscal years 2005 and 2004 totaled \$154,058 and \$419,789, respectively. The outstanding balance at June 30, 2005, totaled \$68,549.

Public Employees' Retirement System-DBRP Education Fund: Education is provided to all members of the PERS regardless of plan choice as governed by section 19-3-112, MCA. The education must be presented with impartial and balanced information about plan choices, investments and retirement planning. The education program consists of three primary components:

1) initial transfer education - complete as of July 1, 2003;

- 2) ongoing transfer education for new hire members after the July 1, 2002 plan start date; and
- 3) ongoing investment/retirement planning education for all active members.

The education program was funded by 0.04% of PERS-covered payroll in fiscal year 2005 the same as fiscal year 2004.

Actuarial Status: The statutory funding rate is tested in the valuation to determine if it is sufficient to cover the Normal Cost Rate plus an amortization payment of the Unfunded Actuarial Liability, if any, over no more than 30 years. Based on the current Actuarial Value of Assets and all future experience emerging as assumed, Unfunded Actuarial Liability will not be amortized over the next 30 years. In general, the deterioration of the funded status is primarily due to recognizing prior investment losses due to returns less than the long-term assumed rate of 8% per year. Based on the actuarial assumptions as of June 30, 2005, an additional funding rate of 1.58% of payroll would be required to fund the current and projected benefits from the DB plan in accordance with GASB standards and state law.

Judges' Retirement System (JRS)

Plan Description: The JRS is a single-employer defined benefit plan established in 1967, and governed by Title 19, chapters 2 & 5 of the MCA. This system provides benefits for all Montana judges of the district courts, justices of the Supreme Court, and the Chief Water Judge. Benefits are established by state law and can only be amended by the Legislature. The JRS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibil-

ity, years of service and compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits is on the following page:

JRS Summary of Benefits

Member's current salary or highest average compensation (HAC)2

¹Hired prior to July 1, 1997 and non-GABA — monthly compensation at time of retirement; ²Hired after June 30, 1997 or electing GABA — HAC during any consecutive 36 months

Eligibility for benefit

Age 60, 5 years of membership service;

Any age with 5 years of membership service - involuntary termination, actuarially reduced

Vesting 5 years of membership service

Monthly benefit formula

3 1/3% of current salary (non-GABA) or HAC (GABA) per year of service credit for the first 15 years, plus 1.785% per year for each year after 15 years

Guaranteed Annual Benefit Adjustment (GABA)

Hired after July 1, 1997, or those electing GABA - after the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit

Minimum benefit adjustment (non-GABA)

Hired prior to July 1, 1997 - current salary is used in the calculation of the monthly benefit each time the Legislature increases salaries for active judges.

At June 30, 2005 JRS had one participating employer, the same as FY2004. The participating employer consists of:

JRS E	MPLOYERS	
Employer	June 30, 2005	June 30, 2004
State Agency - Supreme Court	<u>1</u>	<u>1</u>
Total	1	1

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal years 2005 and 2004 was 7.0% of the member's monthly compensation. Contributions are deducted from each member's salary and remitted by the participating employer. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. As

the employer, the State contributed 25.81% of the total JRS-covered payroll to the retirement plan during fiscal years 2005 and 2004. (Reference Schedule of Contribution Rates on page A-63).

JRS Membership by Employee Type				
Employee Type	June 30, 2005	June 30, 2004		
GABA	25	15		
Non-GABA	25	35		
Total	50	50		

Highway Patrol Officers' Retirement System (HPORS)

Plan Description: The HPORS is a singleemployer, defined benefit plan established July 1, 1971, and governed by Title 19, chapters 2 & 6 of the MCA. This system provides retirement benefits to all members of the Montana Highway Patrol, including supervisory personnel. Benefits are established by state law and can only be amended by the Legislature. The HPORS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits follows:

HPORS Summary of Benefits

Member's highest average compensation (HAC)

Highest average compensation during any consecutive 36 months

Eligibility for benefit

20 years of membership service, regardless of age;

Early Retirement

5 years of membership service, actuarially reduced from age 60

Vesting 5 years of membership service

Monthly benefit formula

2.5% of HAC per year of service credit

Guaranteed Annual Benefit Adjustment (GABA)

Hired after July 1, 1997, or those electing GABA - after the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit

Minimum benefit adjustment (non-GABA)

Hired prior to July 1, 1997 - monthly benefits for non-GABA members are increased each July when they fall below a statutorily guaranteed minimum. Any annual increase is limited to 5% over the current benefit and may not exceed 60% of the current base salary of a probationary officer.

At June 30, 2005 HPORS had one participating employer, the same as FY2004. The participating employer consists of:

	HPORS EMPLOYERS		-"
<u>Employer</u>		June 30, 2005	June 30, 2004
State Agency - Dept. of Justice		<u>1</u>	<u>1</u>
Total		1	1

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rates for fiscal years 2005 and 2004 are 9.05% of the member's total compensation if hired after June 30, 1997 or for members electing GABA and 9.0% for those members hired prior to July 1, 1997 and not electing GABA (All members hired prior to July 1,1997 have elected the GABA). Contributions are deducted from each member's salary and remitted by the participating employer. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. As the employer, the State contributed 36.33% of the total HPORS-covered payroll during fiscal years 2005 and 2004. The first 26.15% is payable from the same source used to pay members' compensation. The remaining amount, equal to 10.18%, is payable from a portion of the fees collected from drivers' license and duplicate drivers' license applications. (Reference Schedule of Contribution Rates on page A-63).

HPORS Membership by Employee Type				
Employee Type	June 30, 2005	June 30, 2004		
GABA	201	194		
Non-GABA	0	0		
Total	201	194		

Additional Service Purchase: A provision (19-2-706, MCA) related to the Employee Protection Act allows state and university system employees, who are eligible for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-5" additional service. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. No employees have taken advantage of this provision to date.

Supplemental Benefit: Montana highway patrol officers retired prior to July 1, 1991, or their survivors, may be eligible for an annual supplemental lump-sum payment distributed each September. A portion of each motor vehicle registration fee funds this supplemental benefit. Many factors must be considered for eligibility, including the number of years the recipient has received a benefit and the recipient's age. The average annual supplemental payment in September 2005 was \$2,369. In September 2004, the average annual supplemental payment was \$2,310. This enhancement is available to non-GABA recipients only.

Sheriffs' Retirement System (SRS)

Plan Description: The SRS is a multipleemployer, cost-sharing defined benefit plan established July 1, 1974, and governed by Title 19, chapters 2 & 7, MCA. This plan provides retirement benefits to all Department of Justice criminal investigators hired after July 1, 1993, and to all Montana sheriffs. Benefits are established by state law and can only be amended by the Legislature. The SRS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits follows:

SRS Summary of Benefits

Member's highest average compensation (HAC)

Highest average compensation during any consecutive 36 months

Eligibility for benefit

20 years of membership service, regardless of age;

Early Retirement

Age 50, 5 years of membership service, actuarially reduced

Vesting 5 years of membership service

Monthly benefit formula

2.5% of HAC per year of service credit

Guaranteed Annual Benefit Adjustment (GABA)

After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit

At June 30, 2005 SRS had 56 participating employers, the same as FY2004. The participating employers consist of:

SRS EM	IPLOYERS	
Employers	June 30, 2005	June 30, 2004
State Agencies - Dept. of Justice	1	1
Counties	<u>55</u>	<u>55</u>
Total	56	56

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal years 2005 and 2004 was 9.245% of member's compensation. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. Each employer contributed 9.535% of total SRScovered payroll to the retirement plan during fiscal years 2005 and 2004. (Reference Schedule of Contribution Rates on page A-63).

SRS Membership by Employer Type		
Employer Type	June 30, 2005	June 30, 2004
Dept of Justice	40	37
Counties	640	625
Total	680	662

Additional Service Purchase: A provision (19-2-706, MCA) related to the Employee Protection Act allows state employees, who are eligible for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-

5" additional service. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. As of fiscal year 2005, three employees have taken advantage of this provision since it's inception, the same as in fiscal year 2004. The retirement incentive contributions received (including interest) during fiscal years 2005 and 2004 totaled \$0 and \$4,180, respectively. The outstanding balance at June 30, 2005, totaled \$0.

Actuarial Status: The statutory funding rate is tested in the valuation to determine if it is sufficient to cover the Normal Cost Rate plus an amortization payment of the Unfunded Actuarial Liability, if any, over no more than 30 years. Based on the current Actuarial Value of Assets and all future experience emerging as assumed, the Unfunded Actuarial Liability will not be amortized over the next 30 years. In general, the deterioration of the funded status is primarily due to recognizing prior investment losses due to returns less than the long-term assumed rate of 8% per year. Based on the actuarial assumptions as of June 30, 2005, an additional funding rate of 2.69% of payroll would be sufficient to fund the current and projected benefits from the plan accordance with GASB standards and state law.

Game Wardens' and Peace Officers' Retirement System (GWPORS)

Plan Description: The GWPORS is a multiple-employer, cost-sharing defined benefit plan established in 1963 and is governed by Title 19, chapters 2 & 8, MCA. This system provides retirement benefits to all persons employed as a game warden, warden supervisory personnel, or state peace officer. Benefits are established by state law and can only be amended by the Legislature. The

GWPORS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits is on the following page:

GWPORS Summary of Benefits

Member's highest average compensation (HAC)

Highest average compensation during any consecutive 36 months

Eligibility for benefit

Age 50, 20 years of membership service;

Early Retirement

Age 55, 5 years of membership service

Vesting 5 years of membership service

Monthly benefit formula

2.5% of HAC per year of service credit

Guaranteed Annual Benefit Adjustment (GABA)

After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit

At June 30, 2005 GWPORS had eight participating employers, the same as FY2004. The participating employers consist of:

GWPORS	EMPLOYERS	
Employers	June 30, 2005	June 30, 2004
State Agencies	5	5
Colleges and Universities	<u>3</u>	<u>3</u>
Total	8	8

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal years 2005 and 2004 was 10.56% of member's compensation. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. Each state agency and university employer contributed 9.0% of total GWPORS-covered payroll

to the retirement plan during fiscal years 2005 and 2004. (Reference Schedule of Contribution Rates on page A-63).

GWPORS Membership by Employer			
Employer	June 30, 2005	June 30, 2004	
Dept of Corrections	496	471	
Dept FW&P	94	94	
Dept of Justice	5	6	
Dept of Livestock	28	30	
Dept of Trans.	61	58	
Universities	27	26	
Total	711	685	

Additional Service Purchase: A provision (19-2-706, MCA) related to the Employee Protection Act allows state and university system employees, who are eligible for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-5" additional service. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. No employees have taken advantage of this provision to date.

Actuarial Status: The statutory funding rate is tested in the valuation to determine if it

is sufficient to cover the Normal Cost Rate plus an amortization payment of the Unfunded Actuarial Liability, if any, over no more than 30 years. Based on the current Actuarial Value of Assets and all future experience emerging as assumed, Unfunded Actuarial Liability will not be amortized over the next 30 years. In general, the deterioration of the funded status is primarily due to recognizing prior investment losses due to returns less than the long-term assumed rate of 8% per year. Based on the actuarial assumptions as of June 30, 2005, an additional funding rate of 0.26% of payroll is required to fund the current and projected benefits from the plan in accordance with GASB standards and state law.

Municipal Police Officers' Retirement System (MPORS)

Plan Description: The MPORS is a multiple employer, cost-sharing defined benefit retirement plan established in 1974 and is governed by Title 19, chapters 2 & 9 of the MCA. This plan covers all municipal police officers employed by first- and second-class cities and other cities that adopt the plan. Benefits are established by state law and can only be amended by the Legislature. The MPORS provides retirement, disability and

death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and compensation. Member rights for death and disability are vested immediately. All other rights are vested after five years of service. A brief summary of eligibility and benefits follows:

MPORS Summary of Benefits

Member's final average compensation (FAC)

Hired prior to July 1, 1977 - average monthly compensation of final year of service; Hired after June 30, 1977 - average monthly compensation for last consecutive 36 months

Eligibility for benefit

20 years of membership service, regardless of age;

Early Retirement

Age 50, 5 years of membership service

Vesting 5 years of membership service

Monthly benefit formula

2.5% of FAC per year of service credit

Guaranteed Annual Benefit Adjustment (GABA)

After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit

Minimum benefit adjustment (non-GABA)

If hired before July 1, 1997 and member did not elect GABA, the monthly retirement, disability or survivor's benefit may not be less than ½ the compensation of a newly confirmed officer in the city that the member was last employed.

At June 30, 2005 MPORS had 22 participating employers, the same as in FY2004. The participating employers consist of:

	MPORS EMPLOYERS	
<u>Employers</u>	June 30, 2005	June 30, 2004
Cities and Towns	<u>22</u>	<u>22</u>
Total	22	22

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. Member contribution rates are dependent upon date of hire as a police officer. For fiscal years 2005 and 2004, member contributions as a percentage of salary were 5.8% (if employed on or before June 30, 1975); 7.0% (if employed after June 30, 1975 and prior to July 1, 1979); 8.5% (if employed after June 30, 1979 and prior to July 1, 1997); and, 9.0% (if employed on or after July 1, 1997 and for members electing GABA). Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. Employer contributions to the retirement plan are 14.41% of total MPORScovered payroll. The State contributions are requested at the beginning of the fiscal year based on the previous fiscal year compensation and are due no later than November 1. The State's contribution rate for 2005 and 2004 was 29.37%. (Reference Schedule of Contribution Rates on page A-63).

MPORS Membership by Employee Type		
Employee Type	June 30, 2005	June 30, 2004
GABA	593	591
Non-GABA	12	12
Total	605	603

Deferred Retirement Option Plan (DROP): Beginning July 2002, eligible members of MPORS can participate in the DROP by filing a one-time irrevocable election with the PERB. The DROP is governed by Title 19, chapter 9, part 12, MCA. An eligible member must have completed at least twenty years of membership service. They may elect to participate in the DROP for a minimum of one month and a maximum of

60 months and may participate in the DROP only once. A participant remains a member of the MPORS, but will not receive membership service or service credit in the system for the duration of the member's DROP period. During the participation in the DROP, all mandatory contributions continue to the retirement system. A monthly benefit is calculated based on salary and years of service to the date of the beginning of the DROP period. The monthly benefit is paid into the DROP account until the end of the DROP participation period. At the end of the DROP period, the participant may receive the balance of the DROP account in a lump-sum payment or in a direct rollover to another eligible plan, as allowed by the IRS. If the participant continues employment after the DROP period ends they will again accrue membership service

DROP Participation			
Participants Partici	6/30/2005	6/30/2004	
Participants Beginning of Year	32	27	
Participants Added	9	7	
Completed DROP	6	2	
Participants End of Year	35	32	
DROP Distributions	\$510,348	\$17,663	

and service credit. The DROP account cannot be distributed until employment is formally terminated. As of June 30, 2005, 43 members have participated in the DROP.

Firefighters' Unified Retirement System (FURS)

Plan Description: The FURS is a multipleemployer, cost-sharing defined benefit plan established in 1981, and governed by Title 19, chapters 2 & 13, MCA. This system provides retirement benefits to firefighters employed by first- and second-class cities and other cities that adopt the plan and to firefighters hired by the Montana Air National Guard on or after October 1, 2001. Benefits are established by state law and can only be amended by the Legislature. The FURS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits follows:

FURS Summary of Benefits

Member's compensation

Hired prior to July 1, 1981 and not electing GABA – final monthly compensation (FMC); Hired after June 30, 1981 and those electing GABA - final average compensation (FAC) for last consecutive 36 months

Eligibility for benefit

20 years of membership service, regardless of age;

Early Retirement

Age 50, 5 years of membership service

Vesting 5 years of membership service

Monthly benefit formula

Members hired prior to July 1, 1981 and not electing GABA are entitled to the greater of:

- 2.5% of FAC per year of service, OR
- i) if less than 20 years of service,
 - 2% of FMC for each year of service
- ii) if more than 20 years of service, 50% of the member's FMC plus 2% of the member's FMC for each year of service over 20 years

Members hired after June 30, 1981 and those electing GABA:

2.5% of FAC per year of service

Guaranteed Annual Benefit Adjustment (GABA)

After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit

Minimum benefit adjustment (non-GABA)

If hired before July 1, 1997 and member did not elect GABA, the monthly retirement, disability or survivor's benefit may not be less than ½ the compensation of a newly confirmed firefighter employed by the city that last employed the member (provided the member has at least ten years of service credit).

At June 30, 2005 FURS had 15 participating employers, the same as FY2004. The participating employers consist of:

FURS EMPLOYER	RS	
<u>Employers</u>	June 30, 2005	June 30, 2004
State Agencies - Dept. of Military Affairs	1	1
Cities and Towns	<u>14</u>	<u>14</u>
Total	15	15

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rates for fiscal years 2005 and 2004 are 9.5% for members hired prior to July 1, 1997, and 10.7% for members hired after June 30, 1997 and members electing GABA coverage. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. Employer contribution rates for fiscal years 2005 and 2004 were 14.36% of the total

FURS-covered payroll. The State contribution was 32.61% of total compensation for all covered firefighters in fiscal years 2005 and 2004. State contributions are requested at the beginning of each fiscal year based on previous fiscal year salary and are due no later than November 1. (Reference Schedule of Contribution Rates on page A-63).

FURS Membership by Employee Type						
Employee Type	June 30, 2005	June 30, 2004				
GABA	436	429				
Non-GABA	8	9				
Total	444	438				

Volunteer Firefighters' Compensation Act (VFCA)_

Plan Description: The VFCA is a statewide retirement and disability plan. This compensation plan was established in 1965 and is governed by Title 19, chapters 2 & 17, MCA. All members are unpaid volunteers and the State of Montana is the only contributor to the plan. Benefits are established by state law and can only be amended by the Legislature. The VFCA provides pension, disability and survivorship benefits for all volunteer firefighters who are members of qualified volunteer fire companies in unincorporated areas, towns or villages under the laws of the State of Montana. Benefits are based on eligibility and years of service. Member rights are vested after ten years of credited membership service. VFCA also

provides limited benefits for injuries incurred in the line of duty.

A member can obtain greater than 20 years of service (without being age 55) and when the member retires, a benefit can be drawn on the increased years of service. The maximum years of service allowed is 30 years. For each additional year of service the member's monthly benefit is increased by \$7.50.

A member that chooses to retire and draw a pension benefit may return to service with the volunteer fire department without loss of benefits. A returning member may not be considered an active member. A brief summary of eligibility and benefits follows:

VFCA Summary of Benefits

Eligibility for benefit

Age 55, 20 years of service credit; Age 60, 10 years of service credit

Additional Benefit

After April 25, 2005, members that have greater than 20 years of service credit (with a maximum of 30 years) may receive additional benefits (maximum benefit \$225).

Vesting 10 years of service credit

Monthly benefit formula

\$7.50 per year of service credit, maximum \$150
If greater than 20 years of service credit (but not more than 30 years), maximum \$225

Contributions: The State is the only contributor to the VFCA. Contributions are 5% of fire insurance premium taxes collected on certain fire risks. The State Auditor makes annual payments from the general fund to the Volunteer Firefighters' Pension Fund from fire insurance premiums. (Reference Schedule of Contribution Rates on page A-63).

Group Insurance Payments: Supplemental payments are available to qualified volunteer fire companies that provide additional group medical insurance for their members in case of death or injury incurred while in the line of duty. The payment is made to the volunteer fire companies and is equal to \$75 per year for each mobile firefighting unit owned by the volunteer fire company, up to a maximum of two units.

Public Employees' Retirement System-DCRP (PERS-DCRP)_

Plan Description: The defined contribution retirement plan (DCRP) is a multiple employer plan established July 1, 2002 and governed by Title 19, chapters 2 & 3, MCA. This plan covers eligible employees of the State, university system, local government and certain employees of the school districts that elect the defined contribution retirement plan. All new hires, initially, are members of the PERS-DBRP. New hires have a 12-month window during which they may choose to transfer to the PERS-DCRP or remain in the PERS-DBRP. The choice is irrevocable. Members may not be members of both the defined contribution and defined benefit retirement plans. The PERS-DCRP provides retirement, disability and death benefits to plan members and their beneficiaries. Contribution rates can only be amended by the Legislature. Benefits are based on eligibility and account balance.

The PERB has received a long-term INTER-CAP loan from the Montana Board of Investments through the Montana Department of Administration to fund the plan start-up/implementation costs. Authorization for the loan was provided by the Legislature, Chapter 471, Laws of 1999. As of June 30, 2004, all of the draws have been combined into one loan and the maturity date extended to February 2018. The loan is discussed in Note C of the Financial Section.

The investment options offered within the PERS-DCRP are selected by the PERB with the assistance of the statutorily created Employee Investment Advisory Council and with the advice of a third-party investment analyst. Members of the DCRP decide how to invest their contributions and a portion of their employer's contributions among the of-

fered investment options. The remaining portion of employer's contributions is used to maintain funding of the defined benefit plan, to provide disability benefits and to fund an employee education program. Members are able to invest in any number of the offered investment options and transfer between options. The offered investment options fall into two primary types: (1) the fixed investment option and (2) the variable investment options. The variable investment options cover all standard asset classes and categories and range from aggressive to conservative. The investment options as of June 30, 2005 are as follows:

PERS-DCRP Investment Options

International Stock Funds

American Funds New Perspective SSGA International Growth Opportunities Oakmark International Barclay's Global Equity Index

Small Company Stock Funds Brown Capital Small Co Instl Vanguard Small Cap Index Adm Hotchkis & Wiley Small Cap Value

Mid-Sized Company Stock Funds
Artisan Mid Cap
Janus Mid Cap Value Investors

Large Company Stock Funds
American Funds Growth Fund A
Vanguard Equity-Income Adm
Vanguard Growth & Income Adm

Balanced FundsVanguard Balanced Index

Bond FundsVanguard Total Bond Market Index

Fixed Investment Options DCRP Fixed Fund

Mutual fund administrative costs are not presented on the financial statements. Mutual fund earnings are generally declared net of expenses in accordance with the Securities Exchange Commission and other regulatory authorities. Current reporting standards for mutual companies do not require costs to be made available in the detailed cost reports.

The fixed investment option requires the services of two external providers who were selected through the State's competitive bidding process. The external providers are: Aegon and Pacific Investment Management Company (PIMCO). Aegon provides a guarantee of principal for the fixed assets and sets a quarterly rate of return based upon the investment manager's portfolio yield and duration. PIMCO, the investment manager, directs the investment of fixed assets. Fixed assets are invested in the mutual market in accordance with established guidelines for credit quality, duration and issue concentration.

Fees on the fixed investments are charged by each of the providers. The fees are defined per each contract for specific services rendered. The record keeper, Great West, charges a fixed administrative fee for all plan participants plus a basis point (or percent) fee based on account balances. On a quarterly basis, the contracted record keeper withholds the fees from each plan participant's account. The basis point fees withheld are submitted to the PERB to pay administrative expenses. These amounts are recorded as *Miscellaneous Revenue* in the financial statements.

Administrative expenses and the revenues that fund them are accounted for within the plan. For the PERS-DCRP, the fixed investment is invested in a PIMCO mutual fund and all fees for investment expense are netted from the mutual fund earnings; therefore, the fees are not presented on our financial statements. The fees charged by Great West and Aegon are classified as *Miscellaneous Expense*.

A brief summary of eligibility and benefits follows:

PERS-DCRP Summary of Benefits

Eligibility for Benefit

Termination of service

Vesting

Immediate for member's contributions and attributable income; 5 years for employer's contributions and attributable income

Benefit

Dependent upon individual account balance; IRS permitted rollovers are also possible

At June 30, 2005 PERS-DCRP had 230 reporting employers, one more than in FY2004. The participating employers consist of:

PERS-DCRP EMPLOYERS						
Employers	June 30, 2005	June 30, 2004				
State Agencies	27	28				
Counties	46	44				
Cities and Towns	40	37				
Universities	5	5				
School Districts	79	88				
Other Agencies	<u>33</u>	<u>27</u>				
Total	230	229				

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal year 2005 was 6.9% of PERS-covered payroll, the same as in fiscal year 2004. Contributions are deducted from each member's salary and remitted by participating employers. The entire amount of the member's contribution is credited to the member's retirement account. An individual account is maintained by the thirdparty record keeper. Each state agency and university system employer contributed 6.9% of PERS-covered payroll during fiscal years 2005 and 2004. Participating local governments and school district employers contribute 6.8% of PERS-covered payroll during fiscal years 2005 and 2004. The State contributes the remaining 0.1% for local governments and school employers from the state general fund in fiscal years 2005 and 2004. The employer rate of 6.9% is allocated as follows: 4.19% allocated to the member's retirement account, 2.37% allocated to the defined benefit plan choice rate, 0.04% allocated to defined contribution education fund and 0.3% allocated to the long-term disability plan. (Reference Schedule of Contribution Rates on page A-63).

Plan Membership Elections: Included in the financial statements are employer contribution transfers of \$10,000 and member contribution transfers of \$16,000. These transfers reflect the contribution transfers of DCRP participants that filed elections at or near the June 30th cutoff date but the contributions were moved in early fiscal year 2006.

PERS-DCRP Membership by Employer Type					
Employer Type	June 30, 2005	June 30, 2004			
State Agencies	467	345			
Counties	230	193			
Cities	156	130			
Universities	44	39			
High Schools	0	1			
School Districts	158	144			
Other Agencies	81	63			
Total	1,136	915			

DCRP Education Fund: Implemented July 1, 2002, the DCRP Education Fund (DCEd), as governed by section 19-3-112, MCA, provides education to the members that have joined the PERS-DCRP. The DCEd is funded by 0.04% of the employers' contributions.

DCRP Disability Fund: Implemented July 1, 2002, the DCRP Disability Fund (DC Disability), as governed by section 19-3-2117, MCA, will provide disability benefits to eligi-

ble members of the PERS-DCRP. The DC Disability is funded by 0.3% of the employers' contribution.

Deferred Compensation Plan (457)

Plan Description: The deferred compensation (457) plan is a voluntary supplemental retirement savings plan established in 1976. The deferred compensation plan is governed by Title 19, chapter 50, MCA, in accordance with Internal Revenue Service Code (IRC) §457. All employees of the State, the Montana University System and contracting political subdivisions, are eligible to participate.

Assets of the deferred compensation plan are required to be held in trusts, custodial accounts or insurance company contracts for the exclusive benefit of participants and their beneficiaries. Great West is the third-party record keeper for the deferred compensation plan. Participants elect to defer a portion of their salary, within Internal Revenue Code limits. The deferred salary is not available to employees until separation from service, retirement, death, or upon an unforeseeable emergency while still employed, provided IRS-specified criteria are met.

Plan participants direct their deferred salary into investment options offered within the plan. The investment options offered are selected by the PERB with the assistance of the statutorily-created Employee Investment Advisory Council and with the advice of a third-party investment analyst. Plan participants may invest in as many of the offered investment options as desired. The offered investment options fall into two primary types: (1) the fixed investment option and (2) the variable investment options. The variable investment options

include mutual funds and profile funds. All options range from aggressive to conservative. The mutual funds cover all standard asset classes and categories. The profile funds are preset funds that invest in underlying mutual funds to achieve a set objective such as time horizon or investment style. The investment options as of June 30, 2005 are as follows:

<u>Deferred Compensation (457) Plan</u> <u>Investment Options</u>

International Stock Funds

Artisan International Mutual Discovery Z Templeton Foreign A American Funds New Perspective

Small Company Stock Funds
Neuberger Berman Genesis
RS Diversified Growth

Mid-Sized Company Stock Funds Artisan Mid Cap Investors Hotchkis & Wiley Mid-cap Value

Large Company Stock Funds
Davis NY Venture A
Fidelity Contrafund
TCW Galileo Select Equities N
Vanguard 500 Index
Calvert Social Investors

Balanced Funds
Dodge & Cox Balanced

Bond Funds

Columbia High-Yield PIMCO Total Return Admin

Fixed Investment Options
Montana Fixed Fund

Profile Funds

Aggressive
Moderately Aggressive
Moderate
Moderately Conservative
Conservative

Mutual fund administrative costs are not presented on the financial statements. Mutual fund earnings are generally declared net of expenses in accordance with the Securities Exchange Commission and other regulatory authorities. Current reporting standards for mutual companies do not require costs to be made available in the detailed cost reports.

The fixed investment option guarantees both principal (the deferred salary) and a quarterly rate of return. The fixed investment option requires the services of three external providers who were selected through the State's competitive bidding process. The external providers are: Aegon, Pacific Investment Management Company (PIMCO) and State Street Bank Kansas City (SSKC). Aegon provides a guarantee of principal and sets a quarterly rate of return based upon the investment manager's portfolio yield and duration. PIMCO, the investment manager, directs the investment of fixed assets. Fixed assets are invested in the bond market in accordance with established guidelines for credit quality, duration and issue concentration. SSKC is PIMCO's custodial bank and holder of the fixed assets. SSKC exchanges the assets as directed by PIMCO.

In addition to the above investment options, plan participants previously had the option to direct a portion of their deferrals to a term life insurance policy provided through Allianz Life Insurance. The ability to invest in life insurance is allowed under the IRC and was offered to plan participants prior to life insurance being offered as a standard component of health insurance benefit packages. This investment option has been discontinued; however, plan participants who had previously or originally elected this option may continue.

Fees on the fixed investments are charged by each of the three providers. The fees are defined per each contract for specific services rendered. The record keeper, Great West, charges a fixed administrative fee for all plan participants. The fixed record-keeping fee, by contract, is a flat dollar amount. On a quarterly basis, the contracted record keeper withholds the basis point fee from each plan participant's account. The basis point fees collected are reconciled to the contractual flat dollar amount and any fees withheld in excess of the contractual flat dollar fee are submitted to the PERB. Also submitted to the PERB are 12(b)(1) or re-allotment fees from certain mutual fund companies. These fees are normally charged by the mutual funds for the purpose of individual record keeping. Because the mutual fund companies involved in the deferred compensation plan do not need to keep records of participants' accounts, the fees are returned to the PERB. The PERB uses the excess and 12(b)(1) fees to pay administrative expenses associated with the deferred compensation plan. These amounts are recorded as Miscellaneous Revenue.

Administrative expenses and the revenues that fund them are accounted for within the plan. The fees charged by PIMCO and SSKC for the externally managed fixed investments are classified as *Investment Expense*. The fees

charged by Great West and Aegon are classified as *Miscellaneous Expense*. A brief sum-

mary of eligibility and benefits follows:

Deferred Compensation Plan Summary

Contribution

Voluntary, tax-deferred

Eligibility for Benefit

Not available to participant until separation from service; retirement; death; or upon an unfore-seeable emergency, while still employed, provided IRS-specified criteria are met

Vesting

Participants are fully vested in their accounts at the time of deposit

Benefit

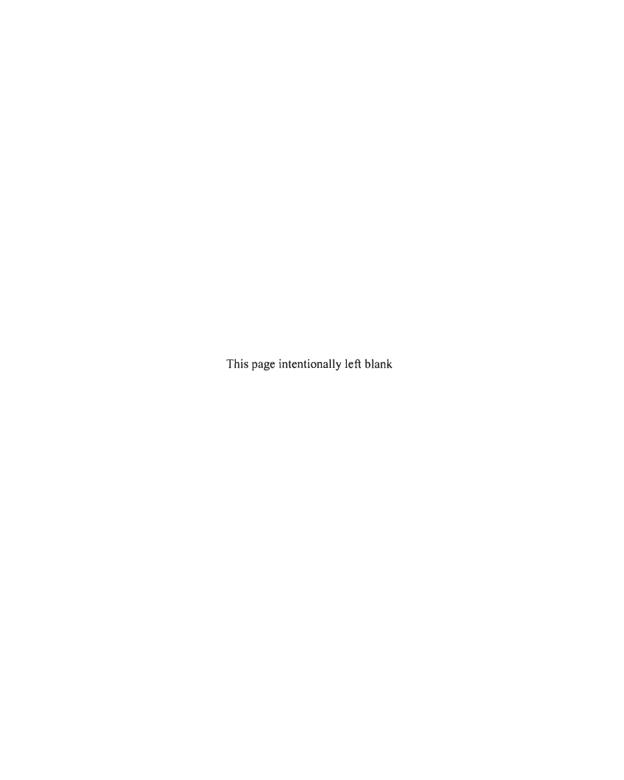
Lump sum or periodic benefit payment, at the option of the participant. Based on individual account balances and plan provisions. IRS permitted rollovers are also possible.

At June 30, 2005 the deferred compensation plan had ten participating employers, an increase of one from FY2004. The participating employers consist of:

DEFERRED COMPENSATION EMPLOYERS					
<u>Employers</u>	June 30, 2005 June 30, 200	<u>4</u>			
State of Montana *	1	1			
Colleges and Universities	6	6			
School Districts	1	0			
Other	<u>2</u>	<u>2</u>			
Total	10	9			
*The State of Montana, includes 35 agencies; however, due to the nature of the reporting for the 457 plan we					

^{*}The State of Montana includes 35 agencies; however, due to the nature of the reporting for the 457 plan we are unable to specifically determine which agencies participate.

Contributions: The deferred compensation plan is a voluntary, tax-deferred retirement plan designed to supplement retirement, Social Security and other retirement plans and savings. Participants designate the amount to contribute within IRC limitations. The deferred salary is withheld through payroll deduction prior to federal and state taxes. Social Security and Medicare taxes are withheld on the deferred salary. The contributions are either directed to the fixed investment or to any number of the available variable investments. The money designated as fixed is invested by PIMCO. The money designated as variable is remitted to the third-party record keeper who in turn invests the contributions in selected investments as directed by the participant.



FY 2005 Schedule of Contribution Rates								
System	Member	Employer	State					
PERS-DBRP	6.9% [19-3-315, MCA]	6.9% State & University 6.8% Local Governments [19-3-316, MCA]	0.1% of local government payroll – paid from the General Fund [19-3-319, MCA]					
PERS-DCRP	6.9% [19-3-315, MCA]	6.9% State & University 6.8% Local Governments [19-3-316, MCA]	0.1% of local government payroll – paid from the General Fund [19-3-319, MCA]					
JRS	7.0% [19-5-402, MCA]	25.81% [19-5-404, MCA]						
HPORS	9.0% - hired prior to 7-01-97 & not electing GABA 9.05% - hired after 6-30-97 & members electing GABA [19-6-402, MCA]	26.15% [19-6-404(1), MCA] 10.18% of salaries – paid from drivers' license fees [19-6-404(2), MCA]						
SRS	9.245% [19-7-403, MCA]	9.535% [19-7-404, MCA]						
GWPORS	10.56% [19-8-502, MCA]	9.0% [19-8-504, MCA]						
MPORS	5.8% - hired on or before 6-30-75 & not electing GABA [19-9-710(a), MCA] 7.0% - hired after 6-30-75 & prior to 7-1-79 & not electing GABA [19-9-710(b), MCA] 8.5% - hired after 6-30-79 and prior to 7-1-97 & not electing GABA [19-9-710(c), MCA] 9.0% - hired after 6-30-97 & members electing GABA [19-9-710(d), MCA]	14.41% [19-9-703, MCA]	29.37% of salaries – paid from the General Fund [19-9-702, MCA]					
FURS	9.5% - hired prior to 7-01-97 & not electing GABA [19-13-601(2)(a), MCA] 10.7% - hired after 06-30-97 & members electing GABA [19-13-601(2)(b), MCA]	14.36% [19-13-605, MCA]	32.61% of salaries – paid from the General Fund [19-13-604, MCA]					
VFCA			5.0% of fire insurance premiums, paid from the General Fund [19-17-301, MCA]					

A Component Unit of the State of Montana

Required Supplementary Information Schedule of Funding Progress

(in thousands)

System	Actuarial Valuation Date	Actuarial Value of Assets ¹ (a)	Actuarial Accrued Liability (AAL) -Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
PERS-DBRP	06/30/00	\$ 2,843,347	\$ 2,273,407	\$ (569,940)	125.07%	\$ 725,692	-78.54%
	06/30/02	3,076,781	3.077.764	983	99.97	808.747	0.12
	06/30/04	3.047.287	3,514,085	466,798	86.72	832,847	56.05
	06/30/05	3,179,010	3,719,998	540,988	85.46	847,431	63.84
JRS	06/30/00	42,043	27,365	(14,678)	153.64	3,483	-421.42
UNO	06/30/02	44.963	30.882	(14,070)	145.60	4,000	-352.03
	06/30/04	45,134	34,724	(10,410)	129,98	4,403	-236.43
	06/30/05	47,552		(13,027)	137.73	4,462	-291.95
HPORS	06/30/00	77,810	76,397	(1,413)	101.85	6,952	-20.33
HFORS	06/30/02	81.734	94,850	13,116	86.17	7,536	174.04
	06/30/02	79,104	104,069	24,965	76.01	7,844	318.27
	06/30/05	82,050	112,938	30,888	72.65	9,104	339.28
SRS	06/30/00	126,338	87,836	(38,502)	143.83	21,559	-178.59
SNS	06/30/00	138,590	121,625	(38,502)	143.83	24,521	-178.59 -69.19
	06/30/02	141.022	148,608	7,586	94.90	27,373	-09.19 27.71
	06/30/05	148,458	159,347	10,889	93.17	28,423	38.31
	00/30/03	140,400	135,347	10,003	73.17	20,423	30.31

Analysis of the dollar amounts of plan net assets, actuarial accrued liability, and unfunded actuarial accrued provides one indication of the plan's funding status on a going-concern basis. Analysis of this percentage percentage, the stronger the plan. Trends in the unfunded actuarial accrued liability and annual covered covered payroll approximately adjusts for the effects of inflation and aids analysis of the plan's progress stronger the plan.

¹Refer to the "Notes to the Required Supplementary Information" for the Actuarial Asset Valuation Method (Page A-68).

²This schedule reflects a subsequent letter from Milliman, MPERA's actuary, dated January 20, 2003. If the actual rates of termination were used for the corrections officers that transferred into the GWPORS the Funded Status of the system would have been a slight Actuarial Surplus rather than a slight Unfunded Actuarial Liability.

System	Actuarial Valuation Date	Actuarial Value of Assets ¹ (a)	Actuarial Accrued Liability (AAL) -Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
GWPORS	06/30/00	\$ 32,966	\$ 23,922	\$ (9,044)	137.81%	11,875	-76.16%
om one	06/30/02 ²	38,730	38,340	. , ,	101.02	17,151	-2.27
	06/30/02	45,210	50,310	, ,	89.86	21,442	23.79
	06/30/05	50,961	56,414	The state of the s	90.33	22,496	24.24
MPORS	06/30/00	129,826	181,109	51,283	71.68	20,252	253.22
	06/30/02	143,516	226,827	83,311	63.27	22,229	374.79
	06/30/04	149,510	260,094	110,584	57.48	24,531	450.79
	06/30/05	159,417	276,379	116,962	57.68	26,198	446.45
FURS	06/30/00	123,492	162,329	38,837	76.08	16.549	234.68
IONO	06/30/02	136,392	197,946		68.90	17,953	342.86
	06/30/02	142,109	227.599		62.44	20,248	422.21
	06/30/05	151,393	238,157	and the second s	63.57	20,474	423.78
VFCA	06/30/00	17,769	16,752	(1,017)	106.07	N/A	N/A
	06/30/02	19,254	26,808	7,554	71.82	N/A	N/A
	06/30/04	20,058	28,680	8,622	69.94	N/A	N/A
	06/30/05	21,311	30,773	and the second s	69.25	N/A	N/A

Covered payroll is not applicable to VFCA because members are unpaid volunteers.

liability in isolation can be misleading. Expressing plan net assets as a percentage of the actuarial accrued liability over time indicates whether the plan is becoming financially stronger or weaker. Generally, the greater this payroll are both affected by inflation. Expressing the unfunded actuarial accrued liability as a percentage of annual made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the

A Component Unit of the State of Montana

Required Supplementary Information Schedule of Employer Contributions & Other Contributing Entities

	Year	Annual	I	Actuarial Required			Annual Required	
	Ended	Require	d	Contribution	Percentage		State	Percentage
System	June 30	Contributi	ons	Rate ¹	Contributed	Cor	tribution 2	Contributed
PERS-	2000	\$ 27,503	3,741	3.79%	177.16%	\$	347,560	100.00%
DBRP	2001	29,238		3.79	181.98		382,481	100.00
	2002	55,803	3,545	6.90	99.54		373,721	100.00
	2003	58,573	3,696	6.90	98.16		388,954	100.00
	2004	67,044	,215	8.05	86.20		402,566	100.00
	2005	71,523	3,156	8.44	82.06	1 /5	420,658	100.00
JRS	2000	608	3,195	17.46	147.82			
	2001	638	3,282	17.46	147.82			
	2002	801	,137	20.03	128.86			
	2003	816	3,691	20.03	128.86			
	2004	304	1,277	6.91	373.52			
	2005	143	3,222	3.21	811.43			
HPORS	2000	602	2,731	8.67	424.30		279,577	100.00%
	2001	637	7,399	8.67	414.48		335,107	100.00
	2002	2,737	7,999	36.33	101.16		308,973	100.00
	2003	2,836	5,992	36.33	101.02		353,589	100.00
	2004	2,849	,545	36.33	100.32		348,137	100.00
	2005	3,307	7,439	36.33	100.50		668,748	100.00
SRS	2000	1,592	2,161	7.39	137.95			
	2001	1,672		7.39	133.17			
	2002	2,338		9.54	102.10			
	2003	2,435	5,269	9.54	102.70			
	2004	3,198	3,485	11.69	84.57			
	2005	3,474	1,750	12.23	80.95	139 150	STATE OF THE PARTY	SE SECO

Refer to the "Notes to the Required Supplementary Information" (Page A-68).

This schedule was revised in FY2005 to reflect the actuarially calculated ARC rather than the statutory rate that was previously

¹ The Annual Required Contribution for FY01 and FY03 is based on prior year-end actuarial study.

²The Annual Required Contribution for HPORS includes the required registration fees and for MPORS and FURS is based on covered payroll, which includes payroll adjustments.

System	Year Ended June 30	Annual Required Contributions	Actuarial Required Contribution Rate	Percentage Contributed	Annual Required State Contribution ²	Percentage Contributed
GWPORS	2000	\$ 642,434	5.41%	171.22%		
GWPORS	2000	805,073	5.41%	169.66		
	2001	1,759,644	10.26	90.64		
	2002	2,055,590	10.26	89.28		
	2003	1,979,117	9.23	102.12		
	2004	2,083,154	9.26	98.58	PRODUCT BOX	NOW THE REAL PROPERTY.
	2005	2,003,134	5.20	80.30		
MPORS	2000	2,918,274	14.41	100.57	\$ 5,947,932	99.35%
	2001	3,011,475	14.41	100.12	6,137,893	100.16
	2002	3,203,173	14.41	102.15	6,528,604	100.02
	2003	3,355,991	14.41	104.89	6,840,073	
	2004	3,534,920	14.41	102.68	7,204,760	
	2005	3,775,191	14.41	100.41	7,694,474	100.14
FURS	2000	2,376,392	14.36	97.86	5,396,528	97.80
10110	2001	2,401,328	14.36	98.81	5,453,155	
	2002	2,578,021	14.36	97.80	5,854,406	
	2002	2,672,133	14.36	106.04	6,068,123	
	2004	2,876,584	14.36	100.09	6,532,410	
	2005	2,940,092	14.36	100.65	6,676,629	THE RESIDENCE OF THE PARTY OF T
VFCA	2000				961,306	100.00
	2001				1,002,992	
	2002				1,133,741	
	2002				1,133,741	
	2003				1,434,068	
	2005		// S S S S S S S S S S	The state of the s	1,527,264	WITH THE PARTY OF STREET STREET

A Component Unit of the State of Montana

Notes to the Required Supplementary Information

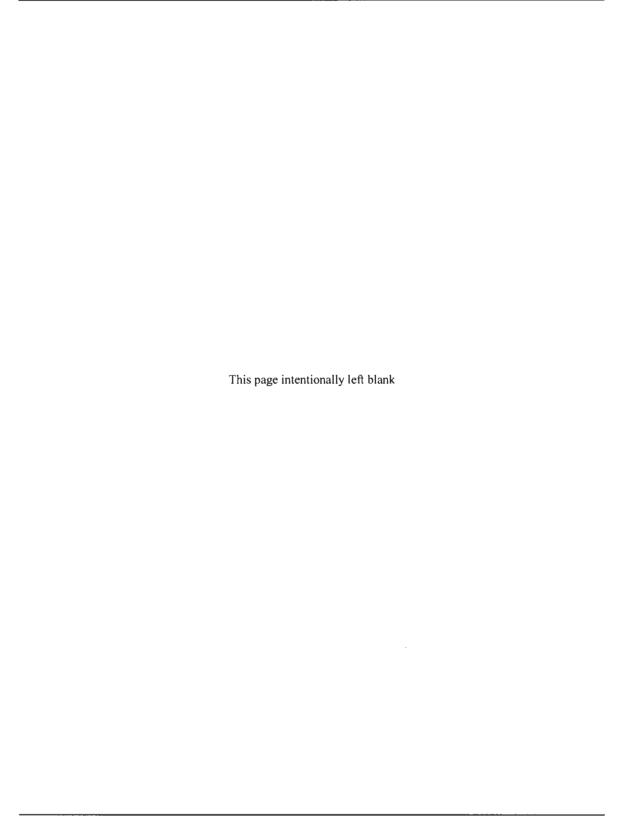
The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of latest actuarial valuation follows:

	PERS-DBRP	JRS	HPORS
Valuation date	June 30, 2005	June 30, 2005	June 30, 2005
Actuarial cost method	Entry Age	Entry Age	Entry Age
Amortization method	Level percentage of payroll, open	Level percentage of payroll, open	Level percentage of payroll, open
Remaining amortization period in years:	The Carlot		THE REAL PROPERTY.
Unfunded Liability	does not amortize		21.1
Unfunded Credit ²		30	
Asset valuation method	4-Year smoothed market	4-Year smoothed market	4-Year smoothed market
Actuarial assumptions:			
Investment rate of return compounded			
annually	8%	8%	8%
Projected salary increases		150	all all property and the
General Wage Growth*	4.25%	4.25%	4.25%
Merit	0% - 6%	None	0% - 7.3%
* includes inflation rate at	3.25%	3.25%	3.25%
Benefit Adjustments	COMPONE S		
GABA	3% after 1 yr	3% after 1 yr	3% after 1 yr
Non-GABA	N/A	Annual increase to salary of active member in like position	2% per yr service for newly confirmed officer

¹ The amortization period for the unfunded actuarial liability in the PERS, SRS and GWPORS exceeds 40 years. Based on actuarial assumptions as of June 30, 2005, additional funding is required at a rate of 1.58% for PERS, 2.69% for SRS and 0.26% for GWPORS. The PERB anticipates legislation to be enacted within fiscal year 2006 to actuarially fund the systems.

² Assets are larger than the past service liability – creating an unfunded credit; the credit is amortized over future costs.

SRS	GWPORS	MPORS	FURS	VFCA
June 30, 2005				
Entry Age				
Level percentage of payroll, open	Level percentage of revenue, open			
does not amortize ¹	does not amortize	23.9	17.6	20
4-Year smoothed market				
8%	8%	8%	8%	8%
4.25%	4.25%	4.25%	4.25%	N/A
0% - 7.3%	0% - 7.3%	0% - 7.3%	0% - 7.3%	N/A
3.25%	3.25%	3.25%	3.25%	N/A
3% after 1 yr	N/A			
N/A	N/A	50% newly confirmed officer	50% newly confirmed officer	N/A



A Component Unit of the State of Montana

Supporting Schedule Schedule of Administrative Expenses Year Ended June 30, 2005

	Defined Benefit Plans	Edu	S-DBRP cation und	Defined Contribution PERS-DCRP		Deferred Compensation 457 Plan	
Personal Services							
Salaries	\$ 1,022,675	\$	66,681	\$	86,767	\$	91,643
Board Members' Per Diem	5,546				527		527
Employee Benefits	301,671		17,921		25,451		24,966
Total Personal Services	1,329,892		84,602		112,745		117,136
Other Services							
Consulting Services	291,180		129		23,177		84,717
Legal Fees and Court Costs	37,640				29		29
Payroll Fees	871		34		77		65
Audit Fees	13,839				442		442
Medical Services	20,921						
Microfilming							
Records Storage	10,617		27		10		8
Pre-Retirement Seminars			2,000				
Computer Processing	254,797		1,172		6,408		2,513
Printing and Photocopy Charges	26,287		10,908		1,097		3,437
Warrant Writing Services	30,348				969		969
Other	15,031		584		4,609		4,396
Total Other Services	701,531		14,854		36,818		96,576
Communications							
Recruitment Costs	7						
Postage and Mailing	90,954		13,366		1,417		14,154
Telephone	22,274		1,109		1,938		1,630
Total Communications	113,235		14,475		3,355		15,783
Other Expenses							
Supplies and Materials	40,315		1,901		5,468		5,027
Travel	21,567		7,914		4,128		4,678
Rent	185,794		9,383		16,407		13,782
Repairs and Maintenance	1,840		64		139		117
Depreciation/Amortization	299,281				3,039		40,698
Compensated Absences	16,240		1,866		(11, 136)		(8,723)
Interest Payments					43,743		
Miscellaneous	36,542		(9,752)		15,976		4,141_
Total Other Expenses	601,579		11,376		77,764		59,720
Total Administrative Expenses	\$ 2,746,237	\$	125,307	\$	230,682	\$	289,215

A Component Unit of the State of Montana Supporting Schedule Schedule of Investment Expenses Year Ended June 30, 2005

Plan	Investment Manager	_	Fees
PERS-DBRP	Board of Investments	\$	4,778,075
JRS	Board of Investments		68,429
HPORS	Board of Investments		119,992
SRS	Board of Investments		213,745
GWPORS	Board of Investments		68,381
MPORS	Board of Investments		219,939
FURS	Board of Investments		209,361
VFCA	Board of Investments		29,820
457	PIMCO State Street Bank		415,575 45,308
Total Investment Expense	9	\$	6,168,625

A Component Unit of the State of Montana Supporting Schedule

Schedule of Consultants
Year Ended June 30, 2005

Individual or Firm	Nature of Service	Amount Paid
Wisetek Provider Inc	Web Reporting Systems Development	\$ 173,862
Milliman Inc	Actuarial Consultant	110,569
Amdec Sofware	Computer Programming Services	78,855
Ice Miller	Tax Consultant	43,003
Mellon Consultants Inc	Actuarial Consultant	37,000
Arnerich Massena & Associates, Inc.	Mutual Funds Performance Review	34,838
Goetz, Gallik, Baldwin & Dolan	Legal Services	26,990
Legislative Audit Division, Legislative Branch	Independent Auditors	14,723
Lawrence R. McEvoy, MD	Medical Consultant	9,574
Legal Services Division, Department of Justice	Legal Services	7,517
Professional Development Center, Department of Administration	Retirement Planning Seminars	2,000

A Component Unit of the State of Montana **Detail of Fiduciary Net Assets** (PERS-DBRP and PERS-DBEd)

as of June 30, 2005

	PERS-DBRP	PERS-DBEd	TOTAL
Assets			
Cash and Short-term Investments	\$ 58,804,818	\$ 994,025	\$ 59,798,843
Securities Lending Collateral	140,879,522		140,879,522
Receivables			and the second
Interest	7,466,205		7,466,205
Accounts Receivable	1,423,537	6	1,423,543
Due from Other Funds	281,669	11,457	293,126
Due from Primary Government	135,867		135,867
Advances to Other Funds			and the same of
Notes Receivable	166,912		166,912
Total Receivables	9,474,190	11,463	9,485,653
Investments, at fair value			
Montana Domestic Equity Pool (MDEP)	1,529,417,961		1,529,417,961
Retirement Fund Bond Pool (RFBP)	930,369,190		930,369,190
Montana International Pool (MTIP)	505,111,709		505,111,709
Montana Private Equity Pool (MPEP)	150,594,503		150,594,503
Equity Index Fund	140		140
Real Estate Investments	8,525,400		8,525,400
Mortgages & Commercial Loans			
net of Accumulated Mortgage Discount	50,658,046		50,658,046
Total Investments	3,174,676,949		3,174,676,949
Capital Assets			
Property and Equipment, at cost,			
net of Accumulated Depreciation	975		975
Intangible Assets, at cost,			THE PARTY OF THE P
net of Amortization Expense	318,975		318,975
Total Capital Assets	319,950		319,950
Total Assets	3,384,155,429	1,005,488	3,385,160,917
Liabilities			
Securities Lending Collateral Liability	140,879,522		140,879,522
Accounts Payable	434,688	4,866	439,554
Due to Other Funds	56,493	195	56,688
Due to Primary Government	44,352	1,982	46,334
Deferred Revenue	55,488		55,488
Compensated Absences	253,478		264,458
Total Liabilities	141,724,021	18,023	141,742,044
Net Assets Held in Trust for Pension Benefits*	\$ 3,242,431,408	\$ 987,465	\$ 3,243,418,873

A Component Unit of the State of Montana

Detail of Changes in Fiduciary Net Assets (PERS-DBRP and PERS-DBEd)

for the Fiscal Year Ended June 30, 2005

		PERS-DBRP		PERS-DBEd		TOTAL	
Additions				-	20		
Contributions							
Employer	\$	59,971,094	\$	325,995	\$	60,297,089	
Plan Member		66,913,560			200	66,913,560	
Membership Fees		140			333	140	
Interest Reserve Buyback		72,550			1	72,550	
Retirement Incentive Program		154,058				154,058	
Miscellaneous Revenue		2,716		95	3.00	2,811	
State Contributions		420,658				420,658	
Total Contributions		127,534,776		326,090	1	127,860,866	
Investment Income							
Net Appreciation (Depreciation)					500		
in Fair Value of Investments		151,817,678			500	151,817,678	
Interest		77,914,976		20,078		77,935,054	
Dividends		19,775,193				19,775,193	
Investment Expense		(4,778,075)				(4,778,075)	
Net Investment Income		244,729,772		20,078	6	244,749,850	
Securities Lending Income							
Securities Lending Income		3,224,315				3,224,315	
Securities Lending Rebate and Fees		(2,998,456)			300	(2,998,456)	
Net Securities Lending Income		225,859				225,859	
Total Net Investment Income		244,955,631		20,078	60 0	244,975,709	
Total Additions		372,490,407		346,168		372,836,575	
Deductions					1		
Benefits		142,789,016			2	142,789,016	
Refunds/Distributions		13,236,058			100	13,236,058	
Refunds to Other Plans		441,716			800	441,716	
Transfers to DCRP		914,334			100	914,334	
Transfers to ORP		158,616				158,616	
Administrative Expenses		2,444,078		125,307		2,569,385	
Total Deductions		159,983,818		125,307		160,109,125	
Net Increase (Decrease)		212,506,589		220,861		212,727,450	
Net Assets Held in Trust for Pension Benefits					100		
Beginning of Year	3	3,029,909,610	_	769,203	1	3,030,678,813	
Prior Period Adjusment		12,610				12,610	
End of Year	\$ 3	3,242,428,809	\$	990,064	\$	3,243,418,873	

A Component Unit of the State of Montana

Detail of Fiduciary Net Assets (PERS-DCRP, PERS-DCEd and PERS-DC Disability) as of June 30, 2005

						ERS-DC		
	PE	RS-DCRP	PEI	RS-DCEd	DI	SABILITY		TOTAL
Assets								
Cash and Short-term Investments	\$	208,131	\$	52,859	\$	287,295	\$	548,285
Receivables							10.00	
Accounts Receivable		14						14
Due from Other Funds		55,030		196		1,462		56,688
Total Receivables		55,044		196		1,462	12.00	56,702
Investments, at fair value							511	
Defined Contributions Fixed Investments		1,545,772					1000	1,545,772
Defined Contributions Variable Investments		23,401,771						23,401,771
Total Investments		24,947,543						24,947,543
Intangible Assets, at cost,		· -						7 The wall
net of Amortization Expense		4,464						4,464
Total Assets		25,215,182		53,055		288,757	9	25,556,994
Liabilities							100	
Accounts Payable		13,308						13,308
Due to Other Funds		2,697		11,950			200	14,647
Due to Primary Government		30,697						30,697
Advances from Primary Government		1,380,195					1537	1,380,195
Advances from Other Funds							1530	
Compensated Absences		8,697		104				8,801
Total Liabilities		1,435,594		12,054			6	1,447,648
Net Assets Held In Trust for Pension Benefits	\$	23,779,588	\$	41,001	\$	288,757	\$	24,109,346

Public Employees' Retirement Board

A Component Unit of the State of Montana

Detail of Changes in Fiduciary Net Assets (PERS-DCRP, PERS-DCEd and PERS-DC Disability) for the Fiscal Year Ended June 30, 2005

			PERS-DC	
	PERS-DCRP	PERS-DCEd	DISABILITY	TOTAL
Additions				
Contributions				
Employer	\$ 1,702,996	\$ 34,935	\$ 118,509	\$ 1,856,440
Plan Member	3,183,893			3,183,893
Miscellaneous Revenue	178,431			178,431
Forfeiture of Nonvested Member	192,257			192,257
Total Contributions	5,257,577	34,935	118,509	5,411,021
Investment income				
Net Appreciation (Depreciation)				The second second
in Fair Value of Investments	1,112,489			1,112,489
Interest	649,481	968	5,212	655,661
Net Investment Income	1,761,970	968	5,212	1,768,150
Total Additions	7,019,547	35,903	123,721	7,179,171
Deductions				
Refunds to Members	1,873,378			1,873,378
Administrative Expenses	218,079	12,603		230,682
Miscellaneous Expenses	255,844			255,844
Total Deductions	2,347,301	12,603	· · · · · · · · · · · · · · · · · · ·	2,359,904
Net Increase (Decrease)	4,672,246	23,300	123,721	4,819,267
Net Assets Held in Trust for Pension Benefits				
Beginning of Year	19,115,270	17,701	165,074	19,298,045
Prior Period Adjustment	(7,928)		(38)	(7,966)
End of Year	\$ 23,779,588	\$ 41,001	\$ 288,757	\$ 24,109,346

Board Response

PUBLIC EMPLOYEE RETIREMENT ADMINISTRATION



BRIAN SCHWEITZER GOVERNOR

STATE OF MONTANA:

(406) 444-3154

TELEFAX (406) 444-5428 TOLL FREE (877) 275-7372 100 N. PARK, SUITE 200 PO BOX 200131 HELENA, MONTANA 59620-0131

November 23, 2005

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LEGISLATIVE AUDIT DIV.

Scott A. Seacat, Legislative Auditor Legislative Audit Division Room 160, State Capitol PO Box 201705 Helena MT 59620-1705

Dear Mr. Seacat,

We have reviewed the recommendation pertaining to the Financial Audit of the Public Employees' Retirement Board (PERB) for the fiscal year ended June 30, 2005:

Recommendation #1

We recommend legislation be enacted for funding changes to ensure the PERS-DBRP, SRS, and the GWPORS are funded on an actuarially sound basis, as required by the Montana Constitution and state law.

Response

We concur. Public retirement systems are required to be actuarially sound as required by the Montana Constitution. If retirement systems are determined not to be actuarially sound, then action is required by the legislature to maintain the actuarial soundness of all public retirement systems.

According to the PERB's Actuarial Valuations as of July 1, 2004 and July 1, 2005 the actuarial soundness of the PERS-DBRP, SRS and GWPORS needs to be addressed by the legislature. Based on the 2004 valuation, Montana's Constitution and the PERB's Benefit and Funding Policy the PERB introduced legislation that addressed this recommendation in the 2005 Legislative Session; however, no legislation was passed to correct the funding problem. There was a joint resolution of the Senate and the House of Representatives requesting a legislative study on how public employee retirement funds are invested and how investment performance, retirement plan benefits, and legislative policy decisions interact to affect the actuarial soundness of the public employee retirement plans and employer's funding obligations. This study was effective April 27, 2005 and assigned to the State Administration and Veteran's Affairs Interim Committee (SAVA).

The PERB has worked with the SAVA Committee to develop legislation addressing the funding issue. There has been discussion of combining an infusion of money and phasing in an increase in employer rates beginning July 1, 2006.

Sincerely,

Mike O'Connor

Executive Director